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Message from the Secretary to the Treasury

I am extrmely pleased to note that the Public Sector Accounting Sandards Commitlee of CA Sri Lanka with the participation of Auditor General's Department and the Ministry of Finance has formulated this 3rd volume of ten Sri Lanka Public Sector Accounting Standards (SLPSAS) wich is based on the International Public Sector Accounting standards (IPSAS) making a total of twenty sandards in 3 volumues.

These accrual based standards provide a frame work for quality accounting and reporting facilitating reliable information for decision making in the Public Sector in line with the international best practises. These standards are currently applicable to Statutory Boards (Non - Commercial Public Corporations) and Local Authorities which are following accrual based accounting. The Central Government and Provincial Councils coud apply these standards once they move to accrual accounting system.

Publication of these standards will facilitate the Government's financial reporting reforms in a manner to strengthen the initiatives to good govemance including transparency and accountability.

I wish to take this opportunity to espress my sincere appreciation and gratitude to CA Sri Lanka and its Public Sector Wing for the efforts taken in this regard.

Dr. R. H. S. Samaraunga
Secretary to the Treasury

Message from the President of CA Sri Lanka

The public sector in Sri Lanka plays a very critical anchor role in the economic development and progress of Sri Lanka, and as the national body of accountants in the country, CA Sri Lanka has taken every effort necessary to help enhance the standing of the accounting and financial professionals who are working in this sector.

With the objective to enhance the professional skills and expertise of public sector accountants and other financial professionals, CA Sri Lanka together with its Public Sector Wing (APFASL) launched a series of initiatives to help propel public sector accountants, auditors & assessors in an effort to elevate their professional standing. Among the key initiatives taken was to publish Sri Lanka Public Sector Accounting Standards (SLPSAS) and this has been a continuous process where SLPSAS has been issued to ensure our public sector professionals are in line with international standards.

The first volume of the Sri Lanka Public Sector Accounting Standards containing four SLPSAS was issued in 2009, followed by the issuance of another six SLPSAS in the second volume. This third volume which has been formulated jointly with the Ministry of Finance and with support from the Asian Development Bank (ADB) contains ten standards, totaling the public sector standards to 20 standards, which is a remarkable feat.

As the sole authority in the country to promulgate accounting and auditing standards, CA Sri Lanka wants the exceptional standards practiced in the private sector also replicated in the public sector, by ensuring this sector too is in line with the best of both national and international standards. Therefore, every effort will be taken to consistently improve this sector, and ensure the public sector in Sri Lanka is second to none.

On behalf of the Council of CA Sri Lanka, I would like to take this opportunity to appreciate the dedicated work performed by the members of the Public Sector Accounting Standards Committee, as well as the officials of the Ministry of Finance and ADB for supporting this important effort.

Lasantha Wickremasinghe
President
CA Sri Lanka

Forward:

We are pleased to release this 3rd volume of the Sri Lanka Public Sector Accounting standards (SLPSAS) containing ten standards formulated jointly with the Ministry of Finance with the support of the Asian Development Bank. These ten standards have been selected on the need basis from the International Public Sector Accounting Standards (IPSAS) and adopted with the permission of the International Federation of Accountants. (IFAC) following due process similar to those adopted for the 1st two volumes of ten standards. We now have altogether twenty standards.

These standards are expected to bring about high quality financial statements in the public sector reflecting fair view of financial performance, position and cash flows promoting uniformity and comparability providing reliable information for decision making.

Considering the complexities of these standards the Association of Public Finance Accountants (APFASL), the Public Sector wing of CA Sri Lanka is in the process of creating awareness and building capacity through various training programmes to facilitate implementation.

Preparation and presentation of Financial Statements in compliance with these standards will enhance financial reporting practices in the Public Sector ensuring Transparency Accountability and Good Governance.

I take this opportunity to express my sincere thanks and gratitude to the Secretary and members of the Public Sector Accounting Standards Committee and the consultant who assisted in formulating these standards. I would also like to take this opportunity to place on record the financial assistance provided by the Asian Development Bank and the commitments and support extended by the President and the Council of CA Sri Lanka to this endeavour.

V. Kanagasabapathy

V. Kanagasabapathy
President, Association of Public Finance Accountants of Sri Lanka
Chairman Public Sector Accounting Standards Committee

CONTENTS

SLPSAS – 11- Revenue from Non- Exchange

Transactions (Taxes & Transfers)

Acknowledgement

Revenue from Non-Exchange Transactions (Taxes and Transfers) (SLPSAS – 11) of the “Sri Lanka Public Sector Accounting Standards – Volume III” is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 11-REVENUE FROM NON-EXCHANGE TRANSACTIONS (TAXES AND TRANSFERS)

CONTENTS

Sri Lanka Public Sector Accounting Standard 11, Revenue from Non-Exchange Transactions (Taxes and Transfers), is set out in paragraphs 1–125. All the paragraphs have equal authority. SLPSAS 11 should be read in the context of its objective, and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe requirements for the financial reporting of revenue arising from non-exchange transactions, other than non-exchange transactions that give rise to an entity combination. This Standard deals with issues that need to be considered in recognizing and measuring revenue from non-exchange transactions, including the identification of contributions from owners.

Scope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for revenue from non-exchange transactions. This Standard does not apply to an entity combination that is a non-exchange transaction.**

3. **This Standard applies to all public sector entities other than Government Business Enterprises.**

4. The *Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements*.

5. This Standard addresses revenue arising from non-exchange transactions. Revenue arising from exchange transactions is addressed in SLPSAS 10, *Revenue from Exchange Transactions*. While revenues received by public sector entities arise from both exchange and non-exchange transactions, the majority of revenue of governments and other public sector entities is typically derived from non-exchange transactions, such as:

   (a) Taxes; and

   (b) Transfers (whether cash or noncash), including grants, debt forgiveness, fines, bequests, gifts, donations, goods and services in kind.

6. Governments may reorganize the public sector, merging some public sector entities, and dividing other entities into two or more separate entities. An entity combination occurs when two or more reporting entities are brought together to form one reporting entity. These restructurings do not ordinarily involve one entity purchasing another entity, but may result in a new or existing entity acquiring all the assets and liabilities of another entity. The PSASC has not addressed entity combinations, and has excluded them from the scope of this Standard. Therefore, this Standard does not specify whether an entity combination, which is a non-exchange transaction, will give rise to revenue or not.

Definitions

7. **The following terms are used in this Standard with the meanings specified:**

Conditions on transferred assets are stipulations that specify that the future economic benefits or service potential embodied in the asset is required to be consumed by the recipient as specified or future economic benefits or service potential must be returned to the transferor.

Control of an asset arises when the entity can use or otherwise benefit from the asset in pursuit of its objectives, and can exclude or otherwise regulate the access of others to that benefit.

Expenses paid through the tax system are amounts that are available to beneficiaries regardless of whether or not they pay taxes.

Fines are economic benefits or service potential received or receivable by public sector entities, as determined by a court or other law enforcement body, as a consequence of the breach of laws or regulations.

Restrictions on transferred assets are stipulations that limit or direct the purposes for which a transferred asset may be used, but do not specify that future economic benefits or service potential is required to be returned to the transferor if not deployed as specified.

Stipulations on transferred assets are terms in laws or regulation, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity.

Tax expenditures are preferential provisions of the tax law that provide certain taxpayers with concessions that are not available to others.

The taxable event is the event that the government, legislature, or other authority has determined will be subject to taxation.

Taxes are economic benefits or service potential compulsorily paid or payable to public sector entities, in accordance with laws and/or regulations, established to provide revenue to the government. Taxes do not include fines or other penalties imposed for breaches of the law.

Transfers are inflows of future economic benefits or service potential from non-exchange transactions, other than taxes.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of Defined Terms published separately.

Non-Exchange Transactions

8. In some transactions, it is clear that there is an exchange of approximately equal value. These are exchange transactions and are addressed in other SLPSASs.

9. In other transactions, an entity will receive resources and provide no or nominal consideration directly in return. These are clearly non-exchange transactions and are addressed in this Standard. For example, taxpayers pay taxes because the tax law mandates the payment of those taxes. While the taxing government will provide a variety of public services to taxpayers, it does not do so in consideration for the payment of taxes.

10. There is a further group of non-exchange transactions where the entity may provide some consideration directly in return for the resources received, but that consideration does not approximate the fair value of the resources received. In these cases, the entity determines whether there is a combination of exchange and non-exchange transactions, each component of which is recognized separately.

11. There are also additional transactions where it is not immediately clear whether they are exchange or non-exchange transactions. In these cases an examination of the substance of the transaction will determine if they are exchange or non-exchange transactions. For example, the sale of goods is normally classified as an exchange transaction. If, however, the transaction is conducted at a subsidized price, that is, a price that is not approximately equal to the fair value of the goods sold, that transaction falls within the definition of a non-exchange transaction. In determining whether the substance of a transaction is that of a non-exchange or an exchange transaction, professional judgment is exercised. In addition, entities may receive trade discounts, quantity discounts, or other reductions in the quoted price of assets for a variety of reasons. These reductions in price do not necessarily mean that the transaction is a non-exchange transaction.

Revenue

12. Revenue comprises gross inflows of economic benefits or service potential received and receivable by the reporting entity, which represents an increase in net assets/equity, other than increases relating to contributions from owners. Amounts collected as an agent of the government or another government organization or other third parties will not give rise to an increase in net assets or revenue of the agent. This is because the agent entity cannot control the use of, or otherwise benefit from, the collected assets in the pursuit of its objectives.

13. Where an entity incurs some cost in relation to revenue arising from a non-exchange transaction, the revenue is the gross inflow of future economic benefits or service potential, and any outflow of resources is recognized as a cost of the transaction. For example, if a reporting entity is required to pay delivery and installation costs in relation to the transfer of an item of plant to it from another entity, those costs are recognized separately from revenue arising from the transfer of the item of plant. Delivery and installation costs are included in the amount recognized as an asset, in accordance with SLPSAS 7, *Property, Plant, and Equipment*.

Stipulations

14. Assets may be transferred with the expectation and/or understanding that they will be used in a particular way and, therefore, that the recipient entity will act or perform in a particular way. Where laws, regulations, or binding arrangements with external parties impose terms on the use of transferred assets by the recipient, these terms are stipulations, as defined in this Standard. A key feature of stipulations, as defined in this Standard, is that an entity cannot impose a stipulation on itself, whether directly or through an entity that it controls.

15. Stipulations relating to a transferred asset may be either conditions or restrictions. While conditions and restrictions may require an entity to use or consume the future economic benefits or service potential embodied in an asset for a particular purpose (performance obligation) on initial recognition, only conditions require that future economic benefits or service potential be returned to the transferor in the event that the stipulation is breached (return obligation).

16. Stipulations are enforceable through legal or administrative processes. If a term in laws or regulations or other binding arrangements is unenforceable, it is not a stipulation as defined by this Standard. Constructive obligations do not arise from stipulations. SLPSAS 8, Provisions, Contingent Liabilities and Contingent Assets, establishes requirements for the recognition and measurement of constructive obligations.

Conditions on Transferred Assets

17. Conditions on transferred assets (hereafter referred to as conditions) require that the entity either consume the future economic benefits or service potential of the asset as specified, or return future economic benefits or service potential to the transferor in the event that the conditions are breached. Therefore, the recipient incurs a present obligation to transfer future economic benefits or service potential to third parties when it initially gains control of an asset subject to a condition. This is because the recipient is unable to avoid the outflow of resources, as it is required to consume the future economic benefits or service potential embodied in the transferred asset in the delivery of particular goods or services to third parties, or else to return to the transferor future economic benefits or service potential. Therefore, when a recipient initially recognizes an asset that is subject to a condition, the recipient also incurs a liability.

18. As an administrative convenience, a transferred asset, or other future economic benefits or service potential, may be effectively returned by deducting the amount to be returned from other assets due to be transferred for other purposes. The reporting entity will still recognize the gross amounts in its financial statements, that is, the entity will recognize a reduction in assets and liabilities for the return of the asset under the terms of the breached condition,

and will reflect the recognition of assets, liabilities, and/or revenue for the new transfer.

Restrictions on Transferred Assets

19. Restrictions on transferred assets (hereafter referred to as restrictions) do not include a requirement that the transferred asset, or other future economic benefits or service potential, is to be returned to the transferor if the asset is not deployed as specified. Therefore, gaining control of an asset subject to a restriction does not impose on the recipient a present obligation to transfer future economic benefits or service potential to third parties when control of the asset is initially gained. Where a recipient is in breach of a restriction, the transferor, or another party, may have the option of seeking a penalty against the recipient, by, for example, taking the matter to a court or other tribunal, or through an administrative process such as a directive from a government minister or other authority, or otherwise. Such actions may result in the entity being directed to fulfill the restriction or face a civil or criminal penalty for defying the court, other tribunal, or authority. Such a penalty is not incurred as a result of acquiring the asset, but as a result of breaching the restriction.

Substance over Form

20. In determining whether a stipulation is a condition or a restriction, it is necessary to consider the substance of the terms of the stipulation and not merely its form. The mere specification that, for example, a transferred asset is required to be consumed in providing goods and services to third parties or be returned to the transferor is, in itself, not sufficient to give rise to a liability when the entity gains control of the asset.

21. In determining whether a stipulation is a condition or restriction, the entity considers whether a requirement to return the asset or other future economic benefits or service potential is enforceable, and would be enforced by the transferor. If the transferor could not enforce a requirement to return the asset or other future economic benefits or service potential, the stipulation fails to meet the definition of a condition, and will be considered a restriction. If past experience with the transferor indicates that the transferor never enforces the requirement to return the transferred asset or other future economic benefits or service potential when breaches have occurred, then the recipient entity may conclude that the stipulation has the form but not the substance of a condition, and is, therefore, a restriction. If the entity has no experience with the transferor, or has not previously breached stipulations that would prompt the transferor to decide whether to enforce a return of the asset or other future economic benefits or service potential, and it has no evidence to the contrary, it would assume that the transferor would enforce the stipulation and, therefore, the stipulation meets the definition of a condition.

22. The definition of a condition imposes on the recipient entity a performance obligation – that is, the recipient is required to consume the future economic benefits or service potential embedded in the transferred asset as specified, or return the asset or other future economic benefits or service potential to the transferor. To satisfy the definition of a condition, the performance obligation will be one of substance not merely form, and is required as a consequence of the condition itself. A term in a transfer agreement that requires the entity to perform an action that it has no alternative but to perform may lead the entity to conclude that the term is in substance neither a condition nor a restriction. This is because, in these cases, the terms of the transfer itself do not impose on the recipient entity a performance obligation.

23. To satisfy the criteria for recognition as a liability, it is necessary that an outflow of resources will be probable, and performance against the condition is required and is able to be assessed. Therefore, a condition will need to specify such matters as the nature or quantity of the goods and services to be provided or the nature of assets to be acquired as appropriate and, if relevant, the periods within which performance is to occur. In addition, performance will need to be monitored by, or on behalf of, the transferor on an ongoing basis. This is particularly so where a stipulation provides for a proportionate return of the equivalent value of the asset if the entity partially performs the requirements of the condition, and the return obligation has been enforced if significant failures to perform have occurred in the past.

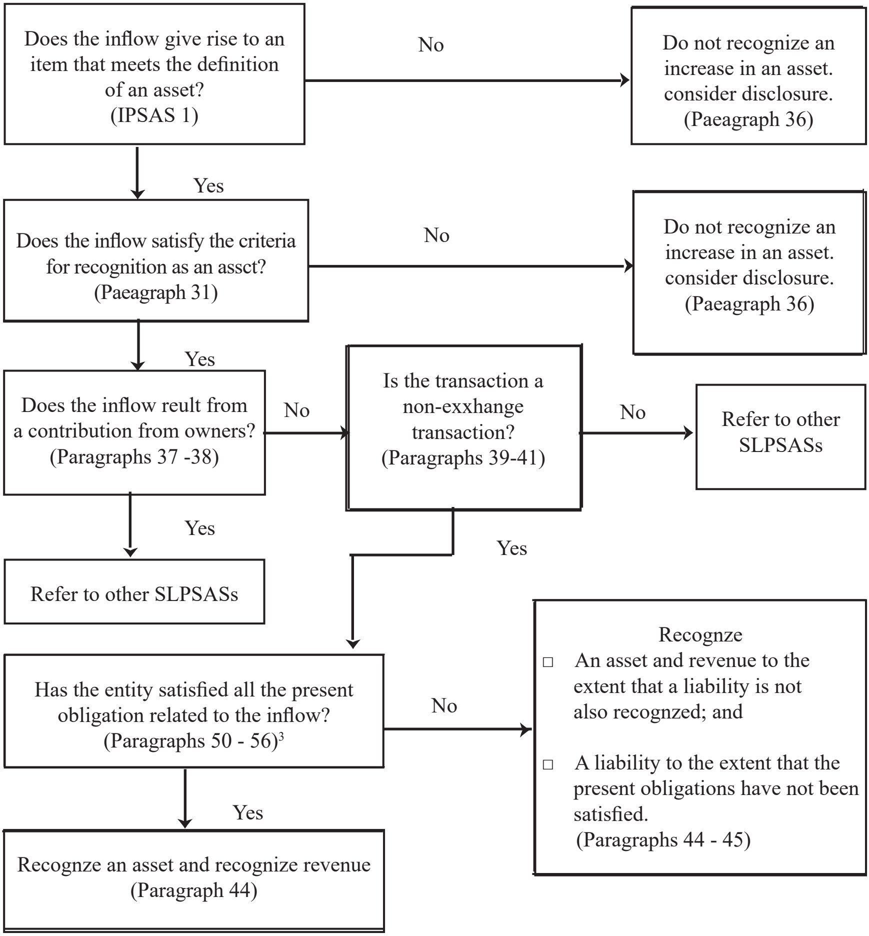
24. In some cases, an asset may be transferred subject to the stipulation that it be returned to the transferor if a specified future event does not occur. This may occur where, for example, a national government provides funds to a provincial council entity subject to the stipulation that the entity raise a matching contribution. In these cases, a return obligation does not arise until such time as it is expected that the stipulation will be breached, and a liability is not recognized until the recognition criteria have been satisfied.

25. However, recipients will need to consider whether these transfers are in the nature of an advance receipt. In this Standard, advance receipt refers to resources received prior to a taxable event or a transfer arrangement becoming binding. Advance receipts give rise to an asset and a present obligation because the transfer arrangement has not yet become binding. Where such transfers are in the nature of an exchange transaction, they will be dealt with in accordance with SLPSAS 10.

Taxes

26. Taxes are the major source of revenue for many governments and other public sector entities. Taxes are defined in paragraph 7 as economic benefits compulsorily paid or payable to public sector entities, in accordance with laws or regulation, established to provide revenue to the government, excluding fines or other penalties imposed for breaches of laws or regulation.

Illustration of the Analysis of Initial Inflows of Resources[1]



1. The flowchart is illustrative only, it does not take the place of this Standard. It is provided as an aid to interpreting this Standard.
2. In certain circumstances, such as when a creditor forgives a liability, a decrease in the carrying amount of a previously recognized liability may arise. In these cases, instead of recognizing an asset, the entity decreases the carrying amount of the liability.
3. In determining whether the entity has satisfied all of the present obligations, the application of the definition of conditions on a transferred asset, and the criteria for recognizing a liability, are considered.

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[1]The flowchart is illustrative only; it does not take the place of this Standard. It is provided as an aid to interpreting this Standard.

Noncompulsory transfers to the government or public sector entities such as donations and the payment of fees are not taxes, although they may be the result of non-exchange transactions. A government levies taxation on individuals and other entities, known as taxpayers, within its jurisdiction by use of its sovereign powers.

27. Tax laws and regulations can vary significantly from jurisdiction to jurisdiction, but they have a number of common characteristics. Tax laws and regulations (a) establish a government's right to collect the tax, (b) identify the basis on which the tax is calculated, and (c) establish procedures to administer the tax, that is, procedures to calculate the tax receivable and ensure payment is received. Tax laws and regulations often require taxpayers to file periodic returns to the government agency that administers a particular tax. The taxpayer generally provides details and evidence of the level of activity subject to tax, and the amount of tax receivable by the government is calculated. Arrangements for receipt of taxes vary widely but are normally designed to ensure that the government receives payments on a regular basis without resorting to legal action. Tax laws are usually rigorously enforced and often impose severe penalties on individuals or other entities breaching the law.

28. Advance receipts, being amounts received in advance of the taxable event, may also arise in respect of taxes.

Analysis of the Initial Inflow of Resources from Non-Exchange Transactions

29. An entity will recognize an asset arising from a non-exchange transaction when it gains control of resources that meet the definition of an asset and satisfy the recognition criteria. In certain circumstances, such as when a creditor forgives a liability, a decrease in the carrying amount of a previously recognized liability may arise. In these cases, instead of recognizing an asset, the entity decreases the carrying amount of the liability. In some cases, gaining control of the asset may also carry with it obligations that the entity will recognize as a liability. Contributions from owners do not give rise to revenue, so each type of transaction is analyzed, and any contributions from owners are accounted for separately. Consistent with the approach set out in this Standard, entities will analyze non-exchange transactions to determine which elements of general purpose financial statements will be recognized as a result of the transactions. The flow chart on the following page illustrates the analytic process an entity undertakes when there is an inflow of resources to determine whether revenue arises. This Standard follows the structure of the flowchart. Requirements for the treatment of transactions are set out in paragraphs 30–115.

Recognition of Assets

30. Assets are defined in SLPSAS 1 as resources controlled by an entity as a

result of past events, and from which future economic benefits or service potential are expected to flow to the entity.

31. **An inflow of resources from a non-exchange transaction, other than services in-kind, that meets the definition of an asset shall be recognized as an asset when, and only when:**

    (a) It is probable that the future economic benefits or service potential associated with the asset will flow to the entity; and

    (b) The fair value of the asset can be measured reliably.

Control of an Asset

32. The ability to exclude or regulate the access of others to the benefits of an asset is an essential element of control that distinguishes an entity's assets from those public goods that all entities have access to and benefit from. In the public sector, governments exercise a regulatory role over certain activities, for example, financial institutions or pension funds. This regulatory role does not necessarily mean that such regulated items meet the definition of an asset of the government, or satisfy the criteria for recognition as an asset in the general purpose financial statements of the government that regulates those assets. In accordance with paragraph 98, entities may, but are not required, to recognize services in-kind.

33. An announcement of an intention to transfer resources to a public sector entity is not of itself sufficient to identify resources as controlled by a recipient. For example, if a public school were destroyed by a forest fire and a government announced its intention to transfer funds to rebuild the school, the school would not recognize an inflow of resources (resources receivable) at the time of the announcement. In circumstances where a transfer agreement is required before resources can be transferred, a recipient entity will not identify resources as controlled until such time as the agreement is binding, because the recipient entity cannot exclude or regulate the access of the transferor to the resources. In many instances, the entity will need to establish enforceability of its control of resources before it can recognize an asset. If an entity does not have an enforceable claim to resources, it cannot exclude or regulate the transferor's access to those resources.

Past Event

34. Public sector entities normally obtain assets from governments, other entities including taxpayers, or by purchasing or producing them. Therefore, the past event that gives rise to control of an asset may be a purchase, a taxable event, or a transfer. Transactions or events expected to occur in the future do not in themselves give rise to assets – hence for example, an intention to levy taxation is not a past event that gives rise to an asset in the form of a

claim against a taxpayer.

Probable Inflow of Resources

35. An inflow of resources is probable when the inflow is more likely than not to occur. The entity bases this determination on its past experience with similar types of flows of resources and its expectations regarding the taxpayer or transferor. For example, where (a) a government agrees to transfer funds to a public sector entity (reporting entity), (b) the agreement is binding, and (c) the government has a history of transferring agreed resources, it is probable that the inflow will occur, notwithstanding that the funds have not been transferred at the reporting date.

Contingent Assets

36. An item that possesses the essential characteristics of an asset, but fails to satisfy the criteria for recognition, may warrant disclosure in the notes as a contingent asset (see SLPSAS 8).

Contributions from Owners

37. Contributions from owners are defined in SLPSAS 1. For a transaction to qualify as a contribution from owners, it will be necessary to satisfy the characteristics identified in that definition. In determining whether a transaction satisfies the definition of a contribution from owners, the substance rather than the form of the transaction is considered. Paragraph 38 indicates the form that contributions from owners may take. If, despite the form of the transaction, the substance is clearly that of a loan or another kind of liability, or revenue, the entity recognizes it as such and makes an appropriate disclosure in the notes to the general purpose financial statements, if material. For example, if a transaction purports to be a contribution from owners, but specifies that the reporting entity will pay fixed distributions to the transferor, with a return of the transferor's investment at a specified future time, the transaction is more characteristic of a loan.

38. A contribution from owners may be evidenced by, for example:

    (a) A formal designation of the transfer (or a class of such transfers) by the contributor or a controlling entity of the contributor as forming part of the recipient's contributed net assets/equity, either before the contribution occurs or at the time of the contribution;

    (b) A formal agreement, in relation to the contribution, establishing or increasing an existing financial interest in the net assets/equity of the recipient that can be sold, transferred, or redeemed; or

    (c) The issuance, in relation to the contribution, of equity instruments that can be sold, transferred, or redeemed.

Exchange and Non-Exchange Components of a Transaction

39. Paragraphs 40 and 41 below address circumstances in which an entity gains control of resources embodying future economic benefits or service potential other than by contributions from owners.

40. Paragraph 7 defines exchange transactions and non-exchange transactions, and paragraph 10 notes that a transaction may include two components, an exchange component and a non-exchange component.

41. Where an asset is acquired by means of a transaction that has an exchange component and a non-exchange component, the entity recognizes the exchange component according to the principles and requirements of other SLPSASs. The non-exchange component is recognized according to the principles and requirements of this Standard. In determining whether a transaction has identifiable exchange and non-exchange components, professional judgment is exercised. Where it is not possible to distinguish separate exchange and non-exchange components, the transaction is treated as a non-exchange transaction.

Measurement of Assets on Initial Recognition

42. **An asset acquired through a non-exchange transaction shall initially be measured at its fair value as at the date of acquisition.**

43. Consistent with SLPSAS 9, Inventories, SLPSAS 13, Investment Property, and SLPSAS 7, assets acquired through non-exchange transactions are measured at their fair value as at the date of acquisition.

Recognition of Revenue from Non-Exchange Transactions

44. **An inflow of resources from a non-exchange transaction recognized as an asset shall be recognized as revenue, except to the extent that a liability is also recognized in respect of the same inflow.**

45. **As an entity satisfies a present obligation recognized as a liability in respect of an inflow of resources from a non-exchange transaction recognized as an asset, it shall reduce the carrying amount of the liability recognized and recognize an amount of revenue equal to that reduction.**

46. When an entity recognizes an increase in net assets as a result of a non-exchange transaction, it recognizes revenue. If it has recognized a liability in respect of the inflow of resources arising from the non-exchange transaction, when the liability is subsequently reduced, because the taxable event occurs or a condition is satisfied, it recognizes revenue. If an inflow of resources satisfies the definition of contributions from owners, it is not recognized as a liability or revenue.

47. The timing of revenue recognition is determined by the nature of the conditions and their settlement. For example, if a condition specifies that the entity is to provide goods or services to third parties, or return unused funds to the transferor, revenue is recognized as goods or services are provided.

Measurement of Revenue from Non-Exchange Transactions

48. **Revenue from non-exchange transactions shall be measured at the amount of the increase in net assets recognized by the entity.**

49. When, as a result of a non-exchange transaction, an entity recognizes an asset, it also recognizes revenue equivalent to the amount of the asset measured in accordance with paragraph 42, unless it is also required to recognize a liability. Where a liability is required to be recognized it will be measured in accordance with the requirements of paragraph 57, and the amount of the increase in net assets, if any, will be recognized as revenue. When a liability is subsequently reduced, because the taxable event occurs, or a condition is satisfied, the amount of the reduction in the liability will be recognized as revenue.

Present Obligations Recognized as Liabilities

50. A present obligation arising from a non-exchange transaction that meets the definition of a liability shall be recognized as a liability when, and only when:

(a) **It is probable that an outflow of resources embodying future economic benefits or service potential will be required to settle the obligation; and**

(b) **A reliable estimate can be made of the amount of the obligation.**

Present Obligation

51. A present obligation is a duty to act or perform in a certain way, and may give rise to a liability in respect of any non-exchange transaction. Present obligations may be imposed by stipulations in laws or regulations or binding arrangements establishing the basis of transfers. They may also arise from the normal operating environment, such as the recognition of advance receipts.

52. In many instances, taxes are levied and assets are transferred to public sector entities in non-exchange transactions pursuant to laws, regulation, or other binding arrangements that impose stipulations that they be used for particular purposes. For example:

(a) Taxes, the use of which is limited by laws or regulations to specified purposes;

(b) Transfers, established by a binding arrangement that includes conditions:

(i) From national governments to provincial, state or local authorities;

(ii) From state/provincial councils to local authorities;

(iii) From governments to other public sector entities;

(iv) To governmental agencies that are created by laws or regulation to perform specific functions with operational autonomy, such as statutory authorities or regional boards or authorities; and

(v) From donor agencies to governments or other public sector entities.

53. In the normal course of operations, a reporting entity may accept resources prior to a taxable event occurring. In such circumstances, a liability of an amount equal to the amount of the advance receipt is recognized until the taxable event occurs.

54. If a reporting entity receives resources prior to the existence of a binding transfer arrangement, it recognizes a liability for an advance receipt until such time as the arrangement becomes binding.

Conditions on a Transferred Asset

55. **Conditions on a transferred asset give rise to a present obligation on initial recognition that will be recognized in accordance with paragraph 50.**

56. Stipulations are defined in paragraph 7. Paragraphs 14-25 provide guidance on determining whether a stipulation is a condition or a restriction. An entity analyzes any and all stipulations attached to an inflow of resources, to determine whether those stipulations impose conditions or restrictions.

Measurement of Liabilities on Initial Recognition

57. **The amount recognized as a liability shall be the best estimate of the amount required to settle the present obligation at the reporting date.**

58. The estimate takes account of the risks and uncertainties that surround the events causing the liability to be recognized. Where the time value of money is material, the liability will be measured at the present value of the amount expected to be required to settle the obligation. This requirement is in accordance with the principles established in SLPSAS 8.

Taxes

59. **An entity shall recognize an asset in respect of taxes when the taxable event occurs and the asset recognition criteria are met.**

60. Resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of a past event (the taxable event) and expects to receive future economic benefits or service potential from those resources. Resources arising from taxes satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur and their fair value can be reliably measured. The degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition, which includes, but is not limited to, disclosure of the taxable event by the taxpayer.

61. Taxation revenue arises only for the government that imposes the tax, and not for other entities. For example, where the national government imposes a tax that is collected by its taxation agency, assets and revenue accrue to the government, not the taxation agency. Further, where a national government imposes a sales tax, the entire proceeds of which it passes to provincial councils, based on a continuing appropriation, the national government recognizes assets and revenue for the tax, and a decrease in assets and an expense for the transfer to provincial councils. The provincial councils will recognize assets and revenue for the transfer. Where a single entity collects taxes on behalf of several other entities, it is acting as an agent for all of them. For example, where a provincial taxation agency collects income tax for the provincial council and several local authorities, it does not recognize revenue in respect of the taxes collected – rather, the individual authorities that impose the taxes recognize assets and revenue in respect of the taxes.

62. Taxes do not satisfy the definition of contributions from owners, because the payment of taxes does not give the taxpayers a right to receive (a) distributions of future economic benefits or service potential by the entity during its life, or (b) distribution of any excess of assets over liabilities in the event of the government being wound up. Nor does the payment of taxes provide taxpayers with an ownership right in the government that can be sold, exchanged, transferred, or redeemed.

63. Taxes satisfy the definition of non-exchange transaction because the taxpayer transfers resources to the government, without receiving approximately equal value directly in exchange. While the taxpayer may benefit from a range of social policies established by the government, these are not provided directly in exchange as consideration for the payment of taxes.

64. As noted in paragraph 52, some taxes are levied for specific purposes. If the government is required to recognize a liability in respect of any conditions relating to assets recognized as a consequence of specific purpose tax levies,

it does not recognize revenue until the condition is satisfied and the liability is reduced. However, in most cases, taxes levied for specific purposes are not expected to give rise to a liability, because the specific purposes amount to restrictions not conditions.

The Taxable Event

65. Similar types of taxes are levied in many jurisdictions. The reporting entity analyzes the taxation law in its own jurisdiction to determine what the taxable event is for the various taxes levied. Unless otherwise specified in laws or regulations, it is likely that the taxable event for:

    (a) Income tax is the earning of assessable income during the taxation period by the taxpayer;

    (b) (Value-added tax is the undertaking of taxable activity during the taxation period by the taxpayer;

    (c) Goods and services tax is the purchase or sale of taxable goods and services during the taxation period;

    (d) Customs duty is the movement of dutiable goods or services across the customs boundary;

    (e) Death duty is the death of a person owning taxable property; and

    (f) Property tax is the passing of the date on which the tax is levied, or the period for which the tax is levied, if the tax is levied on a periodic basis.

Advance Receipts of Taxes

66. Consistent with the definitions of assets, liabilities, and the requirements of paragraph 59, resources for taxes received prior to the occurrence of the taxable event are recognized as an asset and a liability (advance receipts), because (a) the event that gives rise to the entity's entitlement to the taxes has not occurred, and (b) the criteria for recognition of taxation revenue have not been satisfied (see paragraph 59), notwithstanding that the entity has already received an inflow of resources. Advance receipts in respect of taxes are not fundamentally different from other advance receipts, so a liability is recognized until the taxable event occurs. When the taxable event occurs, the liability is discharged and revenue is recognized.

Measurement of Assets Arising from Taxation Transactions

67. Paragraph 42 requires that assets arising from taxation transactions be measured at their fair value as at the date of acquisition. Assets arising from taxation transactions are measured at the best estimate of the inflow of resources to the entity. Reporting entities will develop accounting policies for the measurement of assets arising from taxation transactions that conform with the requirements of paragraph 42. The accounting policies for estimating

these assets will take account of both the probability that the resources arising from taxation transactions will flow to the government, and the fair value of the resultant assets.

68. Where there is a separation between the timing of the taxable event and collection of taxes, public sector entities may reliably measure assets arising from taxation transactions by using, for example, statistical models based on the history of collecting the particular tax in prior periods. These models will include consideration of the timing of cash receipts from taxpayers, declarations made by taxpayers, and the relationship of taxation receivable to other events in the economy. Measurement models will also take account of other factors such as:

(a) The tax law allowing taxpayers a longer period to file returns than the government is permitted for publishing general purpose financial statements;

(b) Taxpayers failing to file returns on a timely basis;

(c) Valuing non-monetary assets for tax assessment purposes;

(d) Complexities in tax law requiring extended periods for assessing taxes due from certain taxpayers;

(e) The potential that the financial and political costs of rigorously enforcing the tax laws and collecting all the taxes legally due to the government may outweigh the benefits received;

(f) The tax law permitting taxpayers to defer payment of some taxes; and

(g) A variety of circumstances particular to individual taxes and jurisdictions.

69. Measuring assets and revenue arising from taxation transactions using statistical models may result in the actual amount of assets and revenue recognized being different from the amounts determined in subsequent reporting periods as being due from taxpayers in respect of the current reporting period. Revisions to estimates are made in accordance with SLPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*.

70. In some cases, the assets arising from taxation transactions and the related revenue cannot be reliably measured until sometime after the taxable event occurs. This may occur if a tax base is volatile and reliable estimation is not possible. In many cases, the assets and revenue may be recognized in the period subsequent to the occurrence of the taxable event. However, there are exceptional circumstances when several reporting periods will pass before a taxable event results in an inflow of resources embodying future economic benefits or service potential that meets the definition of an asset and satisfies

the criteria for recognition as an asset. For example, it may take several years to determine and reliably measure the amount of death duty due in respect of a large deceased estate because it includes a number of valuable antiques and artworks, which require specialist valuations. Consequently the recognition criteria may not be satisfied until payment is received or receivable.

Expenses Paid Through the Tax System and Tax Expenditures

71. **Taxation revenue shall be determined at a gross amount. It shall not be reduced for expenses paid through the tax system.**

72. In some jurisdictions, the government uses the tax system as a convenient method of paying to taxpayers benefits that would otherwise be paid using another payment method, such as writing a check, directly depositing the amount in a taxpayer's bank account, or settling another account on behalf of the taxpayer. For example, a government may pay part of residents' health insurance premiums, to encourage the uptake of such insurance, either by reducing the individual's tax liability, making a payment by check, or by paying an amount directly to the insurance company. In these cases, the amount is payable irrespective of whether the individual pays taxes. Consequently, this amount is an expense of the government and should be recognized separately in the statement of financial performance. Tax revenue should be increased for the amount of any of these expenses paid through the tax system.

73. Taxation revenue shall not be grossed up for the amount of tax expenditures.

74. In most jurisdictions, governments use the tax system to encourage certain financial behavior and discourage other behavior. For example, in some jurisdictions, homeowners are permitted to deduct mortgage interest and property taxes from their gross income when calculating tax-assessable income. These types of concessions are available only to taxpayers. If an entity (including a natural person) does not pay tax, it cannot access the concession. These types of concessions are called tax expenditures. Tax expenditures are foregone revenue, not expenses, and do not give rise to inflows or outflows of resources – that is, they do not give rise to assets, liabilities, revenue, or expenses of the taxing government.

75. The key distinction between expenses paid through the tax system and tax expenditures is that, for expenses paid through the tax system, the amount is available to recipients irrespective of whether they pay taxes, or use a particular mechanism to pay their taxes. SLPSAS 1 prohibits the offsetting of items of revenue and expense unless permitted by another standard. The offsetting of tax revenue and expenses paid through the tax system is not permitted.

Transfers

76. **Subject to paragraph 98, an entity shall recognize an asset in respect of transfers when the transferred resources meet the definition of an asset and satisfy the criteria for recognition as an asset.**

77. Transfers include grants, debt forgiveness, fines, bequests, gifts, donations, and goods and services in-kind. All these items have the common attribute that they transfer resources from one entity to another without providing approximately equal value in exchange, and are not taxes as defined in this Standard.

78. Transfers satisfy the definition of an asset when the entity controls the resources as a result of a past event (the transfer), and expects to receive future economic benefits or service potential from those resources. Transfers satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur, and their fair value can be reliably measured. In certain circumstances, such as when a creditor forgives a liability, a decrease in the carrying amount of a previously recognized liability may arise. In these cases, instead of recognizing an asset as a result of the transfer, the entity decreases the carrying amount of the liability.

79. An entity obtains control of transferred resources either when the resources have been transferred to the entity, or the entity has an enforceable claim against the transferor. Many arrangements to transfer resources become binding on all parties before the transfer of resources takes place. However, sometimes one entity promises to transfer resources, but fails to do so. Consequently only when (a) a claim is enforceable, and (b) the entity assesses that it is probable that the inflow of resources will occur, will assets, liabilities, and/or revenue be recognized. Until that time, the entity cannot exclude or regulate the access of third parties to the benefits of the resources proposed for transfer.

80. Transfers of resources that satisfy the definition of contributions from owners will not give rise to revenue. Agreements (a) that specify that the entity providing resources is entitled to distributions of future economic benefits or service potential during the recipient entity's life, or distribution of any excess of assets over liabilities in the event that the recipient entity is wound up, or (b) that specify that the entity providing resources acquires a financial interest in the recipient entity that can be sold, exchanged, transferred, or redeemed, are, in substance, agreements to make a contribution from owners.

81. Transfers satisfy the definition of non-exchange transactions because the transferor provides resources to the recipient entity without the recipient entity providing approximately equal value directly in exchange. If an agreement stipulates that the recipient entity is to provide approximately equal value in exchange, the agreement is not a transfer agreement, but a contract for an exchange transaction that should be accounted for under SLPSAS 10.

82. An entity analyzes all stipulations contained in transfer agreements to determine if it incurs a liability when it accepts transferred resources.

Measurement of Transferred Assets

83. As required by paragraph 42, transferred assets are measured at their fair value as at the date of acquisition. Entities develop accounting policies for the recognition and measurement of assets that are consistent with SLPSASs. As noted previously, inventories, property, plant, equipment, or investment property acquired through non-exchange transactions are to be initially measured at their fair value as at the date of acquisition, in accordance with the requirements of SLPSAS 9, SLPSAS 13, and SLPSAS 7. Financial instruments, including cash and transfers receivable that satisfy the definition of a financial instrument, and other assets, will also be measured at fair value as at the date of acquisition in accordance with paragraph 42 and the appropriate accounting policy.

Debt Forgiveness and Assumption of Liabilities

84. Lenders will sometimes waive their right to collect a debt owed by a public sector entity, effectively canceling the debt. For example, a national government may cancel a loan owed by a local authority. In such circumstances, the local authority recognizes an increase in net assets because a liability it previously recognized is extinguished.

85. Entities recognize revenue in respect of debt forgiveness when the former debt no longer meets the definition of a liability or satisfies the criteria for recognition as a liability, provided that the debt forgiveness does not satisfy the definition of a contribution from owners.

86. Where a controlling entity forgives debt owed by a wholly owned controlled entity, or assumes its liabilities, the transaction may be a contribution from owners, as described in paragraphs 37-38.

87. Revenue arising from debt forgiveness is measured at the carrying amount of the debt forgiven.

Fines

88. Fines are economic benefits or service potential received or receivable by a public sector entity, from an individual or other entity, as determined by a court or other law enforcement body, as a consequence of the individual or other entity breaching the requirements of laws or regulations. In some jurisdictions, law enforcement officials are able to impose fines on individuals considered to have breached the law. In these cases, the individual will normally have the choice of paying the fine, or going to court to defend the matter. Where a defendant reaches an agreement with a prosecutor that includes the payment of a penalty instead of being tried in court, the payment is recognized as a fine.

89. Fines normally require an entity to transfer a fixed amount of cash to the government, and do not impose on the government any obligations which may be recognized as a liability. As such, fines are recognized as revenue when the receivable meets the definition of an asset and satisfies the criteria for recognition as an asset set out in paragraph 31. As noted in paragraph 12, where an entity collects fines in the capacity of an agent, the fine will not be revenue of the collecting entity. Assets arising from fines are measured at the best estimate of the inflow of resources to the entity.

Bequests

90. A bequest is a transfer made according to the provisions of a deceased person's will. The past event giving rise to the control of resources embodying future economic benefits or service potential for a bequest occurs when the entity has an enforceable claim, for example on the death of the testator, or the granting of probate, depending on the laws of the jurisdiction.

91. Bequests that satisfy the definition of an asset are recognized as assets and revenue when it is probable that the future economic benefits or service potential will flow to the entity, and the fair value of the assets can be measured reliably. Determining the probability of an inflow of future economic benefits or service potential may be problematic if a period of time elapses between the death of the testator and the entity receiving any assets. The entity will need to determine if the deceased person's estate is sufficient to meet all claims on it, and satisfy all bequests. If the will is disputed, this will also affect the probability of assets flowing to the entity.

92. The fair value of bequeathed assets is determined in the same manner as for gifts and donations, as is described in paragraph 97. In jurisdictions where deceased estates are subject to taxation, the tax authority may already have determined the fair value of the asset bequeathed to the entity, and this amount may be available to the entity. Bequests are measured at the fair value of the resources received or receivable.

Gifts and Donations, including Goods In-kind

93. Gifts and donations are voluntary transfers of assets, including cash or other monetary assets, goods in-kind, and services in-kind that one entity makes to another, normally free from stipulations. The transferor may be an entity or an individual. For gifts and donations of cash or other monetary assets and goods in-kind, the past event giving rise to the control of resources embodying future economic benefits or service potential is normally the receipt of the gift or donation. Recognition of gifts or donations of services in-kind are addressed in paragraphs 98–103 below.

94. Goods in-kind are tangible assets transferred to an entity in a non-exchange transaction, without charge, but may be subject to stipulations. External

assistance provided by multilateral or bilateral development organizations often includes a component of goods in-kind.

95. Gifts and donations (other than services in-kind) are recognized as assets and revenue when it is probable that the future economic benefits or service potential will flow to the entity and the fair value of the assets can be measured reliably. With gifts and donations, the making of the gift or donation and the transfer of legal title are often simultaneous; in such circumstances, there is no doubt as to the future economic benefits flowing to the entity.

96. Goods in-kind are recognized as assets when the goods are received, or there is a binding arrangement to receive the goods. If goods in-kind are received without conditions attached, revenue is recognized immediately. If conditions are attached, a liability is recognized, which is reduced and revenue recognized as the conditions are satisfied.

97. On initial recognition, gifts and donations including goods in-kind are measured at their fair value as at the date of acquisition, which may be ascertained by reference to an active market, or by appraisal. An appraisal of the value of an asset is normally undertaken by a member of the valuation profession who holds a recognized and relevant professional qualification. For many assets, the fair value will be readily ascertainable by reference to quoted prices in an active and liquid market. For example, current market prices can usually be obtained for land, non-specialized buildings, motor vehicles and many types of plant and equipment.

Services In-kind

98. **An entity may, but is not required to, recognize services in-kind as revenue and as an asset.**

99. Services in-kind are services provided by individuals to public sector entities in a non-exchange transaction. These services meet the definition of an asset because the entity controls a resource from which future economic benefits or service potential are expected to flow to the entity. These assets are, however, immediately consumed, and a transaction of equal value is also recognized to reflect the consumption of these services in-kind. For example, a public school that receives volunteer services from teachers' aides, the fair value of which can be reliably measured, may recognize an increase in an asset and revenue, and a decrease in an asset and an expense. In many cases, the entity will recognize an expense for the consumption of services in-kind. However, services in-kind may also be utilized to construct an asset, in which case the amount recognized in respect of services in-kind is included in the cost of the asset being constructed.

100. Public sector entities may be recipients of services in-kind under voluntary or non-voluntary schemes operated in the public interest. For example:

(a) Technical assistance from other governments or international organizations;

(b) Persons convicted of offenses may be required to perform community service for a public sector entity;

(c) Public hospitals may receive the services of volunteers;

(d) Public schools may receive voluntary services from parents as teachers' aides or as board members; and

(e) Local governments may receive the services of volunteer fire fighters.

101. Some services in-kind do not meet the definition of an asset because the entity has insufficient control over the services provided. In other circumstances, the entity may have control over the services in-kind, but may not be able to measure them reliably, and thus they fail to satisfy the criteria for recognition as an asset. Entities may, however, be able to measure the fair value of certain services in-kind, such as professional or other services in-kind that are otherwise readily available in the national or international marketplace. When determining the fair value of the types of services in-kind described in paragraph 100, the entity may conclude that the value of the services is not material. In many instances, services in-kind are rendered by persons with little or no training, and are fundamentally different from the services the entity would acquire if the services in-kind were not available.

102. Due to the many uncertainties surrounding services in-kind, including the ability to exercise control over the services, and measuring the fair value of the services, this Standard does not require the recognition of services in-kind. Paragraph 108, however, encourages the disclosure of the nature and type of services in-kind received during the reporting period. As for all disclosures, disclosures relating to services in-kind are only made if they are material. For some public sector entities, the services provided by volunteers are not material in amount, but may be material by nature.

103. In developing an accounting policy addressing a class of services in-kind, various factors would be considered, including the effects of those services in-kind on the financial position, performance, and cash flows of the entity. The extent to which an entity is dependent on a class of services in-kind to meet its objectives, may influence the accounting policy an entity develops regarding the recognition of assets. For example, an entity that is dependent on a class of services in-kind to meet its objectives, may be more likely to recognize those services in-kind that meet the definition of an asset and satisfy the criteria for recognition. In determining whether to recognize a class of services in-kind, the practices of similar entities operating in a similar environment are also considered.

Pledges

104. Pledges are unenforceable undertakings to transfer assets to the recipient entity. Pledges do not meet the definition of an asset, because the recipient entity is unable to control the access of the transferor to the future economic benefits or service potential embodied in the item pledged. Entities do not recognize pledged items as assets or revenue. If the pledged item is subsequently transferred to the recipient entity, it is recognized as a gift or donation, in accordance with paragraphs 93–97 above. Pledges may warrant disclosure as contingent assets under the requirements of SLPSAS 8.

Advance Receipts of Transfers

105. Where an entity receives resources before a transfer arrangement becomes binding, the resources are recognized as an asset when they meet the definition of an asset and satisfy the criteria for recognition as an asset. The entity will also recognize an advance receipt liability if the transfer arrangement is not yet binding. Advance receipts in respect of transfers are not fundamentally different from other advance receipts, so a liability is recognized until the event that makes the transfer arrangement binding occurs, and all other conditions under the agreement are fulfilled. When that event occurs and all other conditions under the agreement are fulfilled, the liability is discharged and revenue is recognized.

Disclosures

106. **An entity shall disclose either on the face of, or in the notes to, the general purpose financial statements:**

(a) **The amount of revenue from non-exchange transactions recognized during the period by major classes showing separately:**

(i) **Taxes, showing separately major classes of taxes; and**

(ii) **Transfers, showing separately major classes of transfer revenue.**

(b) **The amount of receivables recognized in respect of non-exchange revenue;**

(c) **The amount of liabilities recognized in respect of transferred assets subject to conditions;**

(d) **The amount of assets recognized that are subject to restrictions and the nature of those restrictions;**

(e) **The existence and amounts of any advance receipts in respect of non-exchange transactions; and**

(f) **The amount of any liabilities forgiven.**

107. **An entity shall disclose in the notes to the general purpose financial statements:**

(a) **The accounting policies adopted for the recognition of revenue from non-exchange transactions;**

(b) **For major classes of revenue from non-exchange transactions, the basis on which the fair value of inflowing resources was measured;**

(c) **For major classes of taxation revenue that the entity cannot measure reliably during the period in which the taxable event occurs, information about the nature of the tax; and**

(d) **The nature and type of major classes of bequests, gifts, and donations, showing separately major classes of goods in-kind received.**

108. Entities are encouraged to disclose the nature and type of major classes of services in-kind received, including those not recognized. The extent to which an entity is dependent on a class of services in-kind will determine the disclosures it makes in respect of that class.

109. The disclosures required by paragraphs 106 and 107 assist the reporting entity to satisfy the objectives of financial reporting, as set out in SLPSAS 1, which is to provide information useful for decision making, and to demonstrate the accountability of the entity for the resources entrusted to it.

110. Disclosure of the major classes of revenue assists users to make informed judgments about the entity's exposure to particular revenue streams.

111. Conditions and restrictions impose limits on the use of assets, which impacts the operations of the entity. Disclosure of (a) the amount of liabilities recognized in respect of conditions, and (b) the amount of assets subject to restrictions assists users in making judgments about the ability of the entity to use its assets at its own discretion. Entities are encouraged to disaggregate by class the information required to be disclosed by paragraph 106(c).

112. Paragraph 106(e) requires entities to disclose the existence of advance receipts in respect of non-exchange transactions. These liabilities carry the risk that the entity will have to make a sacrifice of future economic benefits or service potential if the taxable event does not occur, or a transfer arrangement does not become binding. Disclosure of these advance receipts assists users to make judgments about the entity's future revenue and net asset position.

113. As noted in paragraph 68, in many cases an entity will be able to reliably measure assets and revenue arising from taxation transactions, using, for example, statistical models. However, there may be exceptional circumstances where an entity is unable to reliably measure the assets and revenue arising until one or more reporting periods has elapsed since the

taxable event occurred. In these cases, the entity makes disclosures about the nature of major classes of taxation that cannot be reliably measured, and therefore recognized, during the reporting period in which the taxable event occurs. These disclosures assist users to make informed judgments about the entity's future revenue and net asset position.

114. Paragraph 107(d) requires entities to make disclosures about the nature and type of major classes of gifts, donations, and bequests it has received. These inflows of resources are received at the discretion of the transferor, which exposes the entity to the risk that, in future periods, such sources of resources may change significantly. Such disclosures assist users to make informed judgments about the entity's future revenue and net asset position.

115. Where services in-kind meet the definition of an asset and satisfy the criteria for recognition as an asset, entities may elect to recognize these services in-kind and measure them at their fair value. Paragraph 108 encourages an entity to make disclosures about the nature and type of all services in-kind received, whether they are recognized or not. Such disclosures may assist users to make informed judgments about (a) the contribution made by such services to the achievement of the entity's objectives during the reporting period, and (b) the entity's dependence on such services for the achievement of its objectives in the future.

Transitional Provisions

116. Entities are not required to change their accounting policies in respect of the recognition and measurement of taxation revenue for reporting periods beginning on a date within five years following the date of first adoption of this Standard.

117. Entities are not required to change their accounting policies in respect of the recognition and measurement of revenue from non-exchange transactions, other than taxation revenue, for reporting periods beginning on a date within three years following the date of first adoption of this Standard.

118. Changes in accounting policies in respect of the recognition and measurement of revenue from non-exchange transactions made before the expiration of the five year period permitted in paragraph 116, or the three year period permitted in paragraph 117, shall only be made to better conform to the accounting policies of this Standard. Entities may change their accounting policies in respect of revenue from non-exchange transactions on a class-by-class basis.

119. When an entity takes advantage of the transitional provisions in paragraph 116 or 117, that fact shall be disclosed. The entity shall also disclose (a) which classes of revenue from non-exchange transactions are recognized in accordance with this Standard, (b) those that have

been recognized under an accounting policy that is not consistent with the requirements of this Standard, and (c) the entity's progress towards implementation of accounting policies that are consistent with this Standard. The entity shall disclose its plan for implementing accounting policies that are consistent with this Standard.

120. When an entity takes advantage of the transitional provisions for a second or subsequent reporting period, details of the classes of revenue from non-exchange transactions previously recognized on another basis, but which are now recognized in accordance with this Standard, shall be disclosed.

121. The transitional provisions are intended to allow entities a period to develop reliable models for measuring revenue from non-exchange transactions during the transitional period. Entities may adopt accounting policies for the recognition of revenue from non-exchange transactions that do not comply with the provisions of this Standard. The transitional provisions allow entities to apply this Standard incrementally to different classes of revenue from non-exchange transactions. For example, entities may be able to recognize and measure property taxes and some classes of transfers in accordance with this Standard from the date of application, but may require up to five years to fully develop a reliable model for measuring income tax revenue.

122. When an entity takes advantage of the transitional provisions in this Standard, its accounting policies for each class of revenue from non-exchange transactions may only be changed to better conform to this Standard. An entity may retain its existing accounting policies until it decides to fully apply the provisions of this Standard, or until the transitional provisions expire, whichever is earlier, or it may change them to apply the requirements of this Standard progressively. An entity may, for example, change from a policy of recognition on a cash basis to a modified cash or modified accrual basis before it fully applies this Standard.

123. The disclosure requirements of paragraph 119 assist users to track the progress of the entity in conforming its accounting policies to the requirements of this SLPSAS during the reporting periods in which the transitional provisions apply. This disclosure facilitates the objective of full accountability and transparency.

Effective Date

124. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1, 2018. Earlier application is encouraged. If an entity applies this Standard for periods beginning before January 1, 2018, it shall disclose that fact.**

125. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Implementation Guidance

This guidance accompanies, but is not part of, SLPSAS 11.

Measurement, Recognition, and Disclosure of Revenue from Non-Exchange Transactions

Income Tax (*paragraph 65*)

IG1. A national government (reporting entity) imposes a 25 percent tax on personal income earned within the country. Employers are required to withhold taxes from payroll and remit withholdings on a monthly basis. Individuals with significant non-salary (for example, investment) income are required to make estimated tax payments on a quarterly basis. In addition, individuals must file a tax return with the taxation department by April 15 of the year following the tax year (calendar year), and must pay the remaining tax owed (or claim a refund) at that time. The government's reporting period ends on June 30.

IG2. The government controls a resource – income tax receivable – when the taxable event occurs, which is the earning of assessable income by taxpayers. At the end of the reporting period, the government recognizes assets and revenue in respect of personal income tax on the income earned during the reporting period, to the extent that it can reliably measure it. Assets and revenue will also be recognized in respect of income taxes on income earned in prior periods, but which did not meet the definition of, or satisfy the criteria for recognition as, an asset until the current reporting period.

Measurement of Taxation Revenue (*paragraphs 67–70*)

IG3. A national government (reporting entity) levies income tax on the personal income of all persons earning income within its jurisdiction. The tax was first levied some seventy years before the current reporting period, and taxation statistics are available for the entire seventy-year period. The tax year and the reporting period are January 1 to December 31. Taxpayers have until April 30 each year to file their tax return, and until June 30 to pay any outstanding taxes. The government is required by legislation to present audited consolidated general purpose financial statements to the legislature no later than March 31.

IG4. Income tax revenue should be recognized in the reporting period in which the taxable event occurred, that is, the earning of taxable income. As the tax administration system does not enable the government to directly measure income tax receivable until after its general purpose financial statements are issued, the government develops a model to indirectly measure income taxation revenue receivable. The government uses the income tax collection history it has in the taxation statistics, which it compares to other observable phenomena to develop a reliable model. Other phenomena can include other economic statistics, such as gross domestic product, financial phenomena such as income tax installments deducted by employers, sales tax collections (if it levies such a tax), and banking statistics collected by the central bank. This government may enlist the assistance of econometricians in developing the model, and the external auditor tests the validity of the model in accordance with international and national auditing standards.

IG5. The model enables the reporting entity to reliably measure the assets and revenue accruing to it during the reporting period, which are then recognized and disclosed in the general purpose financial statements. The notes to the general purpose financial statements disclose the accounting policies, including the basis of measurement of income tax revenue. In these circumstances, estimates of tax revenue for one reporting period may be revised in a subsequent period. Changes in estimates are recognized prospectively in accordance with SLPSAS 3.

Value Added Tax (*paragraph 65*)[1]

IG6. A national government (reporting entity) imposes a value-added tax (VAT) on all businesses. The tax is 15 percent of the value added and is collected by merchants from Rs.stomers (taxpayers) at the time of sale. Large and mediumsized businesses are required to submit VAT returns electronically to the tax department on a weekly basis; however, small businesses are permitted to submit VAT returns manually on a quarterly basis.

IG7. The government controls a resource – VAT receivable – when the taxable event occurs, which is the undertaking of taxable activity, that is, the sale of value-added goods or services, during the reporting period. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which the taxable activity takes place, or later, as soon as it can reliably measure the tax receivable. In many circumstances, the taxation return period will not coincide with the reporting period. In these circumstances, estimates of tax revenue for the reporting period may be revised in a subsequent period. Changes in estimates are recognized prospectively in accordance with SLPSAS 3.

Goods and Services Tax (*paragraph 65*)

IG8. A national government (reporting entity) imposes a goods and services tax (GST) on sales of goods and services. The tax is 10 percent of the value of goods and services sold. Most sellers of goods and services are required to electronically submit GST returns to the tax department on a weekly basis. However, small businesses are permitted to manually submit GST returns on a quarterly basis.

[1]Some jurisdiction use the terms Value Added Tax (VAT) and Goods and Service Tax (GST) interchangeably.

IG9. The government controls a resource – GST receivable – when the taxable event occurs, which is the sale of taxable goods and services during the reporting period. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which the sales and purchases take place or, if the tax receivable cannot be reliably measured as at the end of the reporting period, later, as soon as it can reliably measure the tax receivable.

Customs Duty (*paragraph 65*)

IG10. A national government (reporting entity) imposes customs duty on all imports of goods. The duties vary depending on the type of goods imported, and are set at levels to ensure that domestically produced goods are cheaper in the retail market. Imported goods are held in bonded warehouses until the importer pays the duty. Importers are required to make import declarations to the customs department and pay the duty immediately. Most importers submit these declarations electronically before the goods arrive, and make electronic funds transfers to the customs department when the goods are unloaded from ships or aircraft, or as trains or trucks pass the customs boundary.

IG11. The government controls a resource – duty receivable – when the taxable event occurs, which is the movement of goods across the customs boundary. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which the goods move across the boundary, or later, as soon as it can reliably measure the duty receivable.

Death Duties (*paragraph 65*)

IG12. A national government (reporting entity) imposes death duties of 40 percent on all estates valued at more than 500,000 rupees (Rs.). Medical practitioners and funeral directors are required to notify the tax department of all deaths. An assessor then makes an interim valuation of the estate to determine whether duty will be payable. Executors of estates are required to file an inventory of the estate with the tax department, which values the estate and determines the duty due from the estate. Probate cannot be granted until all duty is paid. Due to complexities in testamentary law and frequent appeals of valuations, it takes on average four years to settle estates and collect the duty due.

IG13. The government controls a resource – death duties receivable – when the taxable event occurs, which is the death of a person owning taxable property. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which the person dies, or later, as soon as it can reliably measure the assets.

Property Tax (*paragraph 65*)

IG14. A local authority (reporting entity) levies a tax of one percent of the assessed value of all property within its jurisdiction. The government's reporting period is July 1 to June 30. The tax is levied on July 31, with notices of assessment being sent to property owners in July, and payment due by August 31. If taxes are unpaid on that date, property owners incur penalty interest rate payments of three percent per month of the amount outstanding. The tax law permits the government to seize and sell a property to collect outstanding taxes.

IG15. The government controls a resource – property taxes receivable – when the taxable event occurs, which is the passing of the date on which the taxes are levied, July 31. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which that date occurs.

Advance Receipts of Income Tax (*paragraph 66*)

IG16. Government A (reporting entity) levies income tax on all residents within its jurisdiction. The tax period and the reporting period are January 1 to December 31. Self-employed taxpayers are required to pay an estimate of their income tax for the year by December 24 of the year immediately preceding the commencement of the tax year. The tax law sets the estimate as the amount due for the most recently completed assessment, plus one tenth, unless the taxpayer provides an explanation prior to December 24 of a lower amount (penalties apply if the taxpayer's assessment proves to be materially lower than the final amount owed). After the end of the tax period, self-employed taxpayers file their tax returns and receive refunds, or pay additional tax to the government.

IG17. The resources received from self-employed taxpayers by December 24 are advance receipts against taxes due for the following year. The taxable event is the earning of income during the taxation period, which has not commenced. The reporting entity recognizes an increase in an asset (cash in bank) and an increase in a liability (advance receipts).

Grant to Another Level of Government for General Purposes (*paragraphs 14–16, 76*)

IG18. The national government (transferor) makes a grant of Rs.10 million to a local authority in a socioeconomically deprived area. The local authority (reporting entity) is required under its constitution to undertake various social programs; however, it has insufficient resources to undertake all of these programs without assistance. There are no stipulations attached to the grant. All local authorities are required to prepare and present audited general purpose financial statements.

IG19. There are no stipulations attached to these grants, and no performance obligation, so the transfers are recognized as assets and revenue in the general purpose financial statements of the reporting period in which they are received or receivable by the local authority.

Transfer with Stipulations that do not Satisfy the Definition of a Condition (*paragraphs 20-25*)

IG20. A national government makes a cash transfer of Rs.50 million to a provincial council social housing entity, specifying that it:

(a) Increases the stock of social housing by an additional 1,000 units over and above any other planned increases; or

(b) Uses the cash transfer in other ways to support its social housing objectives.

If neither of these stipulations is satisfied, the recipient entity must return the cash to the national government.

IG21. The provincial council social housing entity recognizes an increase in an asset (cash) and revenue in the amount of Rs.50 million. The stipulations in the transfer agreement are stated so broadly as to not impose on the recipient a performance obligation – the performance obligation is imposed by the operating mandate of the entity, not by the terms of the transfer.

Transfer to a Public Sector University with Restrictions (*paragraphs 19 and 76*)

IG22. The national government (transferor) transfers 200 hectares of land in a major city to a university (reporting entity) for the establishment of a university campus. The transfer agreement specifies that the land is to be used for a campus, but does not specify that the land is to be returned if not used for a campus.

IG23. The university recognizes the land as an asset in the statement of financial position of the reporting period in which it obtains control of that land. The land should be recognized at its fair value in accordance with SLPSAS 7. The restriction does not meet the definition of a liability or satisfy the criteria for recognition as a liability. Therefore, the university recognizes revenue in respect of the land in the statement of financial performance of the reporting period in which the land is recognized as an asset.

Grant to Another Level of Government with Conditions (*paragraphs 17-18*)

IG24. The national government (transferor) grants Rs.10 million to a provincial council (reporting entity) to be used to improve and maintain mass transit systems. Specifically, the money is required to be used as follows: 40 percent for existing railroad and tramway system modernization, 40 percent for new railroad or tramway systems, and 20 percent for rolling stock purchases and improvements. Under the terms of the grant, the money can only be used as stipulated, and the provincial council is required to include a note in its audited general purpose financial statements detailing how the grant money was spent. The agreement requires the grant to be spent as specified in the current year or be returned to the national government.

IG25. The provincial council recognizes the grant money as an asset. The provincial council also recognizes a liability in respect of the condition attached to the grant. As the province satisfies the condition, that is, as it makes authorized expenditures, it reduces the liability and recognizes revenue in the statement of financial performance of the reporting period in which the liability is discharged.

Research Grant (*in Substance Exchange Transaction*) (*paragraph 8*)

IG26. A large corporation that makes cleaning products (transferor) gives money to a public university (reporting entity) to conduct research on the effectiveness of a certain chemical compound in quickly removing graffiti. The corporation stipulates that the research results are to be shared with it before being announced to the public, and that it has the right to apply for a patent on the compound.

IG27. This is an exchange transaction. In return for the grant, the university provides research services and an intangible asset, the right (a future economic benefit) to profit from the research results. SLPSAS 10 and SLPSAS 20, Intangible Assets apply to this transaction.

Debt Forgiveness (*paragraphs 84-87*)

IG28. The national government (transferor) lent a local authority (reporting entity) Rs.20 million to enable the local authority to build a water treatment plant. After a change in policy, the national government decides to forgive the loan. There are no stipulations attached to the forgiveness of the loan. The national government writes to the local authority and advises it of its decision; it also encloses the loan documentation, which has been annotated to the effect that the loan has been waived.

IG29. When it receives the letter and documentation from the national government, which communicates this decision, the local authority derecognizes the liability for the loan and recognizes revenue in the statement of financial performance of the reporting period in which the liability is derecognized.

Purchase of Property with Exchange and Non-Exchange Components

(*paragraphs 8-11, 39-41*)

IG30. A public school (reporting entity) purchases land with a fair value of Rs.100,000 for Rs.50,000 from a local authority. The reporting entity concludes that the non-exchange transaction comprises two components, an exchange component and a non-exchange component. One component involves the purchase of a half share in the land for Rs.50,000, the other component is a non-exchange transaction that transfers the remaining half share of the land to the school.

IG31. In its general purpose financial statements for the reporting period in which the transaction takes place, the public school recognizes the land at Rs.100,000, (a cost of Rs.50,000 and a transfer of Rs.50,000), a reduction in its asset cash of Rs.50,000, and revenue from a non-exchange transaction of Rs.50,000 (the fair value of the increase in net assets recognized).

Proposed Bequest (*paragraphs 90-92*)

IG32. A 25-year old recent graduate (transferor) of a public university names the university (reporting entity) as the primary beneficiary in her will. This is communicated to the university. The graduate is unmarried and childless and has an estate currently valued at Rs.500,000.

IG33. The public university does not recognize any asset or revenue in its general purpose financial statements for the period in which the will is made. The past event for a bequest is the death of the testator (transferor), which has not occurred.

Pledge—Television Appeal for Public Hospital (*paragraph 104*)

IG34. On the evening of June 30, 20X5, a local television station conducts a fundraising appeal for a public hospital (reporting entity). The annual reporting date of the public hospital is June 30. Television viewers telephone or e-mail, promising to send donations of specified amounts of money. At the conclusion of the appeal, Rs.2 million has been pledged. The pledged donations are not binding on those making the pledge. Experience with previous appeals indicates approximately 75 percent of pledged donations will be made.

IG35. The public hospital does not recognize any amount in its general purpose financial statements in respect of the pledges. The entity does not control the resources related to the pledge, because it cannot exclude or regulate the access of the prospective transferors to the economic benefits or service potential of the pledged resources; therefore it cannot recognize the asset or the related revenue until the donation is binding on the donor.

Fine (*paragraphs 88-89*)

IG36. A major corporation is found guilty of polluting a river. As a penalty, it is required to clean up the pollution and to pay a fine of Rs.50 million. The company is in sound financial condition and is capable of paying the fine. The company has announced that it will not appeal the case.

IG37. The government (reporting entity) recognizes a receivable and revenue of Rs.50 million in the general purpose financial statements of the reporting period in which the fine is imposed.

External Assistance Recognized (*paragraphs 76-82*)

IG38. National Government A (reporting entity) enters into an external assistance agreement with National Government B, which provides National Government A with development assistance grants to support National Government A's health objectives over a two-year period. The external assistance agreement is binding on both parties. The agreement specifies the details of the development assistance receivable by National Government A. Government A measures the fair value of the development assistance at Rs.5 million.

IG39. When the external assistance agreement becomes binding, National Government A recognizes an asset (a receivable) for the amount of Rs.5 million, and revenue in the same amount. The resources meet the definition of an asset and satisfy the recognition criteria when the agreement becomes binding. There are no conditions attached to this agreement that require the entity to recognize a liability.

Revenue of Aid Agency (*paragraphs 76, 93-97*)

IG40. Green-Aid Agency relies on funding from a group of governments. The governments have signed a formal agreement, which determines the percentage of Green-Aid Agency's approved budget that each government will fund. Green-Aid Agency can only use the funds to meet the expenses of the budget year for which the funds are provided. Green-Aid Agency's financial year begins on January 1. Green-Aid Agency's budget is approved in the preceding October, and the invoices are mailed out to the individual authorities ten days after the budget is approved. Some governments pay before the start of the financial year and some during the financial year. However, based on past experience, some governments are very unlikely to pay what they owe, either during the financial year or at any future time.

IG41. For the budget year 20X8, the profile of amounts and timing of payments was as follows:

	(Rs. Million)
Budget approved October 24, 20X7	55
Amount invoiced November 4, 20X7	55
Transfers received as at December 31, 20X7	15
Transfers received during 20X8	38
Amount not received by December 31, 20X8 and unlikely to be received	2

IG42. In 20X7, Green-Aid Agency recognizes an asset of Rs.15 Million for the amount of transfers received before the start of 20X8, because it has control over an asset when the transfer is received and deposited in its bank account. An equivalent Rs.15 Million liability, revenue received in advance, is recognized.

IG43. In 20X8, Green Aid Agency recognizes Rs.53 million of revenue from transfers. In the notes to its general purpose financial statements, it discloses that Rs.55 Million was invoiced and an allowance for doubtful debts of Rs.2 Million was established.

Goods In-kind Recognized as Revenue (*paragraphs 42, 93-97*)

IG44. Transferor Government A has an arrangement with the public sector reporting entity, Aid Agency Inc., whereby Government A provides rice to meet its promised financial commitments to Aid Agency Inc. Based on the variability in Government A's past performance in meeting its commitments, Aid Agency Inc. has adopted an accounting policy of not recognizing the asset and revenue until receipt of the promised rice. Government A promises to provide Aid Agency Inc. with Rs.300,000 during 20X5. Government A subsequently transfers 1,000 metric tons of rice to Aid Agency Inc. on January 12, 20X5. The transfer of the rice takes place in one of the ports of the transferor nation. According to the details of the funding agreement between Aid Agency Inc. and Government A, the rice is valued at the previously agreed amount of Rs.300 per ton, with the result that the transfer of 1,000 metric tons of rice fully discharges Government A's financial commitment of Rs.300,000. During February and March 20X5, Aid Agency Inc. provides the rice to a network of local distribution agencies in Nations B and C in order to meet the needs of starving people.

IG45. On January 12, 20X5, the market price of 1,000 metric tons of rice was: Rs.280,000 in Government A's nation; Rs.250,000 in the international commodities market; Rs.340,000 in recipient Nation B; and Rs.400,000 in recipient Nation C.

IG46. The fair value of the rice at the time of the donation must be determined to measure the revenue that Aid Agency Inc. recognizes. The financial agreement between the donor and the aid agency, which allows the rice to be valued at Rs.300 per metric ton, depends on a private agreement between the two parties, and does not necessarily reflect the fair value of the rice. Both Aid Agency Inc. and Donor Government A have the option of purchasing the rice on the world market at the lower price of Rs.250,000. The market prices for individual countries appear open to fluctuation – either as a result of trade barriers or, in the case of recipient countries, temporary distortions due to severe food shortages, and may not reflect a transfer between a knowledgeable willing buyer and a knowledgeable willing seller in an orderly market. Therefore, the world market price of Rs.250,000 is the most reliable and relevant reflection of fair value for the donated rice. Aid Agency Inc. recognizes an increase in an asset (rice inventory) and revenue of Rs.250,000 in its general purpose financial statements for the year in which the transfer is received.

Disclosure of Services In-kind not Recognized (*paragraphs 98–102, 108*)

IG47. A public hospital's (reporting entity) accounting policies are to recognize voluntary services received as assets and revenue when they meet the definition of an asset and satisfy the criteria for recognition as assets. The hospital enlists the services of volunteers as part of an organized program. The principal aim of the program is to expose volunteers to the hospital environment, and to promote nursing as a career. Volunteers must be at least sixteen years of age, and are initially required to make a six-month commitment to work one four-hour morning or afternoon shift per week. The first shift for each volunteer consists of a hospital orientation training session. Many local high schools permit students to undertake this work as part of their education program. Volunteers work under the direction of a registered nurse and perform non-nursing duties such as visiting patients and reading to patients. The public hospital does not pay the volunteers, nor would it engage employees to perform volunteers' work if volunteers were not available.

IG48. The hospital analyzes the agreements it has with the volunteers and concludes that, at least for a new volunteer's first six months, it has sufficient control over the services to be provided by the volunteer to satisfy the definition of control of an asset. The hospital also concludes that it receives service potential from the volunteers, satisfying the definition of an asset. However, it concludes that it cannot reliably measure the fair value of the services provided by the volunteers, because there are no equivalent paid positions either in the hospital or in other health or community care facilities in the region. The hospital does not recognize the services in-kind provided by the volunteers. The hospital discloses the number of hours of service provided by volunteers during the reporting period and a description of the services provided.

Contribution from Owners (*paragraphs 37-38*)

IG49. In 20X0 the neighboring cities of Altonae, Berolini and Cadomi form the TriCities Electricity Generating Service (TCEGS) (reporting entity). The charter establishing TCEGS is binding on the local authorities and provides for equal ownership, which can only be changed by agreement. The cities contribute Rs.25 million each to establish TCEGS. These contributions satisfy the definition of a contribution from owners, which the entity recognizes as such. The charter also provides for the cities to purchase the output of the TCEGS in proportion to their ownership. The purchase price is equal to the full costs of production. In 20X9, the city of Berolini gives approval for the construction of an aluminum smelter within the city, which will result in a doubling of the city's electricity demand. The three cities agree to amend the charter of TCEGS to permit Berolini to make a contribution from owners to enable the construction of additional generating capacity. After an independent valuation of TCEGS, the cities agree that Berolini may make a Rs.50 million contribution from owners and increase its ownership share to 49.9%, with Altonae and Cadomi retaining 25.05% each.

IG50. When the amendment to the charter becomes binding, TCEGS will recognize an increase in assets of Rs.50 million (cash or contribution from owners receivable) and a contribution from owners of Rs.50 million.

Grant Agreement Term not Requiring Recognition of a Liability (*paragraphs 20-25*)

IG51. National Park Department (reporting entity) of Country A receives a grant of Rs.500,000 from the bilateral aid agency of Country B. The grant agreement stipulates that the grant is required to be used to rehabilitate deforested areas of Country A's existing wilderness reserves, but if the money is not used for the stated purpose, it must be returned to Country B. The terms of the grant agreement are enforceable in the courts of Country A, and in international courts of justice. This is the thirteenth year that National Park Department has received a grant of this type from the same transferor. In prior years, the grant has not been used as stipulated, but has been used to acquire additional land adjacent to national parks for incorporation into the parks. National Park Department has not conducted any rehabilitation of deforested areas in the past thirteen years. Country B's bilateral aid agency is aware of the breach of the agreement term.

IG52. National Park Department analyzes the transaction and concludes that, although the terms of the grant agreement are enforceable, because the bilateral aid agency has not enforced the condition in the past, and given no indication that it ever would, the terms have the form of a stipulation and condition, but not the substance. National Park Department recognizes an increase in an asset (cash in bank) and grant revenue; it does not recognize a liability.

Disclosures Made in the Financial Statements of Government A (*paragraphs 106– 108*)

IG53. For the year ended December 31, 20X2, Government A prepares and presents financial statements prepared in accordance with SLPSASs for the first time. It makes the following disclosures in its financial statements:

REVENUE FROM NON-EXCHANGE TRANSACTION

(TAXES AND TRANSFERS)

Statement of Financial Performance

	20X2 (Rs.',000)	20X1 (Rs.',000)
Revenue from Non-Exchange Transactions		
Taxation Revenue		
Income Tax Revenue (notes 4 and 8)	XXX	XXX
Goods and Services Tax (note 5)	XXX	XXX
Estate Taxes (notes 6 and 9)	XX	XX
Transfer Revenue		
Transfers from Other Governments (note 7)	XXX	XXX
Gifts, Donations, Goods In-kind (note 13)	X	X
Services In-kind (notes 15 and 16)	X	X

Statement of Financial Position

Current Assets		
Cash at Bank	XX	XX
Taxes Receivable		
Goods and Services Taxes Receivable (note 5)	XX	XX
Transfers Receivable		
Transfers receivable from Other Governments (note 7)		X
		X
Noncurrent Assets		
Land (note 11)	XXX	XXX
Plant and Equipment (notes 12 and 14)	XX	XX
Current Liabilities		
Liabilities recognized under transfer arrangements (note 10)	XX	XX
Advance Receipts		
Taxes	X	X
Transfers	X	X

Notes to the Financial Statements

Accounting Policies

Recognition of Revenue from Non-Exchange Transactions

1. Assets and revenue arising from taxation transactions are recognized in accordance with the requirements of SLPSAS 11, Revenue from Non-Exchange Transactions (Taxes and Transfers). However, the Government takes advantage of the transitional provisions in that Standard in respect of income taxes and estate taxes.

   Apart from income taxes and estate taxes, assets and revenue arising from taxation transactions are recognized in the period in which the taxable event occurs, provided that the assets satisfy the definition of an asset and meet the criteria for recognition as an asset. Income taxes and estate taxes are recognized in the period in which payment for taxation is received (see notes 4 and 6).

2. Assets and revenue arising from transfer transactions are recognized in the period in which the transfer arrangement becomes binding, except for some services in-kind. The government recognizes only those services in-kind that are received as part of an organized program and for which it can determine a fair value by reference to market rates. Other services in-kind are not recognized.

3. Where a transfer is subject to conditions that, if unfulfilled, require the return of the transferred resources, the Government recognizes a liability until the condition is fulfilled.

Basis of Measurement of Major Classes of Revenue from Non-Exchange Transactions

Taxes

4. Income tax revenue is measured at the nominal value of cash, and cash equivalents, received during the reporting period. The Government is currently developing a statistical model for measuring income tax revenue on an accruals basis. This model uses taxation statistics compiled since 19X2 as well as other statistical information, including average weekly earnings, gross domestic product, and the consumer and producer price indexes. The Government anticipates that the model will enable it to reliably measure income tax revenue on an accruals basis for the reporting period ended December 31, 20X4. The Government does not recognize any amount in respect of income taxes receivable.

5. Assets and revenue accruing from goods and services tax are initially measured at the fair value of assets accruing to the government during the reporting period, principally cash, cash equivalents, and goods and services tax receivable. The information is compiled from the goods and services tax returns submitted by taxpayers during the year and other amounts estimated

to be due to the government. Taxpayers have a high compliance rate and a low error rate, using the electronic return system established in 20X0. The high compliance and low error rates have enabled the Government to develop a reliable statistical model for measuring the revenue accruing from the tax.

Goods and services taxes receivable is the estimate of the amount due from taxes attributable to the reporting period that remain unpaid at December 31, 20X2, less a provision for bad debts.

6. Estate tax of 40% is levied on all deceased estates; however, the first Rs.400,000 of each estate is exempt from the tax. Assets and revenue from estate taxes are measured at the nominal value of the cash received during the reporting period, or the fair value as at the date of acquisition of other assets received during the period, as determined by reference to market valuations or by independent appraisal by a member of the valuation profession.

Transfer Revenue

7. Assets and revenue recognized as a consequence of a transfer are measured at the fair value of the assets recognized as at the date of recognition. Monetary assets are measured at their nominal value unless the time value of money is material, in which case present value is used, calculated using a discount rate that reflects the risk inherent in holding the asset. Non-monetary assets are measured at their fair value, which is determined by reference to observable market values or by independent appraisal by a member of the valuation profession. Receivables are recognized when a binding transfer arrangement is in place, but cash or other assets have not been received.

Taxes not Reliably Measurable in the Period in which the Taxable Event Occurs

8. The Government is unable to directly measure the assets arising from income tax during the period in which all taxpayers earn income and is, therefore, taking advantage of the transitional provisions of SLPSAS 11, Revenue from Non-Exchange Transactions (Taxes and Transfers), to develop a model to indirectly measure taxation revenue in the period in which taxpayers earn income. The government estimates that it will be able to reliably measure income tax on an accruals basis using the model for the reporting period ending December 31, 20X4.

9. In respect of estate taxes, due to current high levels of noncompliance with the law, the government is unable to measure the amount of assets and revenue accruing in the period in which persons owning taxable property die. The government therefore recognizes estate taxes when it receives payment for the tax. The tax department is continuing work to develop a reliable method of measuring the assets receivable and revenue in the year in which the taxable event occurs.

Liabilities Recognized in Respect of Transfers

10. At December 31, 20X2, the Government recognized a liability of Rs.XX,000 related to a transfer to it conditional upon it building a public hospital. As at December 31, the Government had received a cash payment, however, construction of the hospital had not commenced, although tenders for construction were called for on November 30, 20X2.

Assets Subject to Restrictions

11. Land with a fair value of Rs.XX,000 was donated during 20X2, subject to the restriction that it be used for public health purposes and not be sold for 50 years. The land was acquired by the transferor at a public auction immediately prior to its transfer, and the auction price is the fair value.

12, Plant and equipment includes an amount of Rs.XX,000, which is the carrying amount of a painting donated in 19X2 to an art gallery controlled by the Government, and subject to the restriction that it not be sold for a period of 40 years. The painting is measured at its fair value, determined by independent appraisal.

Major Classes of Bequests, Gifts, Donations, and Goods In-Kind Received

13. Transfers are received in the form of gifts, donations and goods in-kind – most notably medical and school supplies (inventory), medical and school equipment, and works of art (classified as equipment). Gifts and donations are received primarily from private benefactors. Hospitals, schools, and art galleries controlled by the Government recognize these assets when control passes to them, usually on receipt of the resources, either cash or plant and equipment. The Government does not accept these transfers with either conditions or restrictions attached unless the value of the transfer exceeds Rs.XX,000.

14. During 20X2, as part of an external assistance agreement with Government C, computer equipment with a fair value of Rs.XX,000 was provided to the Government on condition that it be used by the education department or be returned to Government C.

Services In-kind

15. Hospitals controlled by the government received medical services in-kind from medical practitioners as part of the medical profession’s organized volunteer program. These services in-kind are recognized as revenue and expenses in the statement of financial performance at their fair value, as determined by reference to the medical profession’s published schedule of fees.

16. Hospitals, schools, and art galleries controlled by the government also received support from volunteers as part of organized programs for art gallery greeters and guides, teachers’ aides, and hospital visitor guides.

These volunteers provide valuable support to these entities in achieving their objectives; however, the services provided cannot be reliably measured as there are no equivalent paid positions available in the local markets and, in the absence of volunteers, the services would not be provided. The government does not recognize these services in the statements of financial position or financial performance.

SLPSAS - 12 - LEASES

Acknowledgement

Leases (SLPSAS - 12) of the "Lanka Public Sector Accounting Standards - Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSAB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 12—LEASES

CONTENTS

Paragraph

Objective

LEASES

Sri Lanka Public Sector Accounting Standard 12, Leases, is set out in paragraphs 1-86. All the paragraphs have equal authority. SLPSAS 12 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

1. The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures to apply in relation to finance and operating leases.

Scope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for all leases other than:**

   (a) **Leases to explore for or use minerals, oil, natural gas, and similar non-regenerative resources; and**

   (b) **Licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents, and copyrights.**

   However, this Standard shall not be applied as the basis of measurement for:

   (a) **Property held by lessees that is accounted for as investment property (see SLPSAS 13, Investment Property);**

   (b) **Investment property provided by lessors under operating leases (see SLPSAS 13);**

   (c) **Biological assets held by lessees under finance leases; or**

   (d) **Biological assets provided by lessors under operating leases.**

3. **This Standard applies to all public sector entities other than Government Business Enterprises.**

4. The *Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

5. This Standard applies to agreements that transfer the right to use assets, even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. This Standard does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other. Public sector entities may enter into complex arrangements for the delivery of services, which may or may not include leases of assets. These arrangements are discussed in paragraphs 25–27.

6. This Standard does not apply to (a) lease agreements to explore for or use natural resources such as oil, gas, timber, metals, and other mineral rights, and (b) licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents, and copyrights. This is because

these types of agreements have the potential to raise complex accounting issues that need to be addressed separately.

7. This Standard does not apply to investment property. Investment properties are measured by lessors and lessees in accordance with the provisions of SLPSAS 13.

Definitions

8. **The following terms are used in this Standard with the meanings specified:**

The commencement of the lease term is the date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial recognition of the lease (i.e., the recognition of the assets, liabilities, revenue, or expenses resulting from the lease, as appropriate).

Contingent rent is that portion of the lease payments that is not fixed in amount, but is based on the future amount of a factor that changes other than with the passage of time (e.g., percentage of future sales, amount of future use, future price indices, future market rates of interest).

Economic life is either:

(a) **The period over which an asset is expected to yield economic benefits or service potential to one or more users; or**

(b) **The number of production or similar units expected to be obtained from the asset by one or more users.**

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.

Gross investment in the lease is the aggregate of:

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

(b) **Any unguaranteed residual value accruing to the lessor.**

Guaranteed residual value is:

(a) **For a lessee, that part of the residual value that is guaranteed by the lessee or by a party related to the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and**

(b) **For a lessor, that part of the residual value that is guaranteed by the lessee, or by a third party unrelated to the lessor, that is financially capable of discharging the obligations under the guarantee.**

The inception of the lease is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease. As at this date:

(a) **A lease is classified as either an operating or a finance lease; and**

(b) **In the case of a finance lease, the amounts to be recognized at the commencement of the lease term are determined.**

Initial direct costs are incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or trader lessors.

The interest rate implicit in the lease is the discount rate that, at the inception of the lease, causes the aggregate present value of:

(a) **The minimum lease payments; and**

(b) **The unguaranteed residual value**

to be equal to the sum of (i) the fair value of the leased asset, and (ii) any initial direct costs of the lessor.

A lease is an agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time.

The lease term is the non-cancelable period for which the lessee has contracted to lease the asset, together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

The lessee's incremental borrowing rate of interest is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.

Minimum lease payments are the payments over the lease term that the lessee is, or can be, required to make, excluding contingent rent, costs for services and, where appropriate, taxes to be paid by and reimbursed to the lessor, together with:

(a) **For a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or**

(b) **For a lessor, any residual value guaranteed to the lessor by:**

   (i) **The lessee;**

   (ii) **A party related to the lessee; or**

(iii) An independent third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.

<u>Net investment in the lease</u> is the gross investment in the lease discounted at the interest rate implicit in the lease.

<u>A non-cancelable lease</u> is a lease that is cancelable only:

(a) **Upon the occurrence of some remote contingency;**

(b) **With the permission of the lessor;**

(c) **If the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or**

(d) **Upon payment by the lessee of such an additional amount that, at inception of the lease, continuation of the lease is reasonably certain.**

<u>An operating lease</u> is a lease other than a finance lease.

<u>Unearned finance revenue</u> is the difference between:

(a) **The gross investment in the lease; and**

(b) **The net investment in the lease.**

<u>Unguaranteed residual value</u> is that portion of the residual value of the leased asset, the realization of which by the lessor is not assured or is guaranteed solely by a party related to the lessor.

<u>Useful life</u> is the estimated remaining period, from the commencement of the lease term, without limitation by the lease term, over which the economic benefits or service potential embodied in the asset are expected to be consumed by the entity.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms* published separately.

Changes in Lease Payments between the Inception of the Lease and the Commencement of the Lease Term

9. A lease agreement or commitment may include a provision to adjust the lease payments (a) for changes in the construction or acquisition cost of

the leased property, or (b) for changes in some other measure of cost or value, such as general price levels, or in the lessor's costs of financing the lease, during the period between the inception of the lease and the commencement of the lease term. If so, the effect of any such changes shall be deemed to have taken place at the inception of the lease for the purposes of this Standard.

Hire Purchase Contracts

10. The definition of a lease includes contracts for the hire of an asset that contain a provision giving the hirer an option to acquire title to the asset upon the fulfillment of agreed conditions. These contracts are sometimes known as hire purchase contracts.

Incremental Borrowing Rate of Interest

11. Where an entity has borrowings that are guaranteed by the government, the determination of the lessee's incremental borrowing rate of interest reflects the existence of any government guarantee and any related fees. This will normally lead to the use of a lower incremental borrowing rate of interest.

Classification of Leases

12. The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. Risks include the possibilities of (a) losses from idle capacity, technological obsolescence, or (b) changes in value because of changing economic conditions. Rewards may be represented by the expectation of service potential or profitable operation over the asset's economic life, and of gain from appreciation in value or realization of a residual value.

13. **A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.**

14. Because the transaction between a lessor and a lessee is based on a lease agreement between them, it is appropriate to use consistent definitions. The application of these definitions to the differing circumstances of the lessor and lessee may result in the same lease being classified differently by them. For example, this may be the case if the lessor benefits from a residual value guarantee provided by a party unrelated to the lessee.

15. Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Although the following are examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease, a lease does not need to meet all these criteria in order to be classified as a finance lease:

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

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

(c) The lease term is for the major part of the economic life of the asset, even if title is not transferred;

(d) At the inception of the lease, the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset;

(e) The leased assets are of such a specialized nature that only the lessee can use them without major modifications; and

(f) The leased assets cannot easily be replaced by another asset.

16. Other indicators that individually or in combination could also lead to a lease being classified as a finance lease are:

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

(b) Gains or losses from the fluctuation in the fair value of the residual accrue to the lessee (for example in the form of a rent rebate equaling most of the sales proceeds at the end of the lease); and

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

17. The examples and indicators in paragraphs 15 and 16 are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. For example, this may be the case (a) if ownership of the asset transfers at the end of the lease for a variable payment equal to its then fair value, or (b) if there are contingent rents as a result of which the lessee does not have substantially all such risks and rewards.

18. Lease classification is made at the inception of the lease. If at any time the lessee and the lessor agree to change the provisions of the lease, other than by renewing the lease, in a manner that would have resulted in a different classification of the lease under the criteria in paragraphs 12–17 if the changed terms had been in effect at the inception of the lease, the revised agreement is regarded as a new agreement over its term. However, changes in estimates (for example, changes in estimates of the economic life or the residual value of the leased property) or changes in circumstances (for example, default by the lessee), do not give rise to a new classification of a lease for accounting purposes.

19. [Not used to maintain consistency of paragraph numbers with IPSASs]

20. [Not used to maintain consistency of paragraph numbers with IPSASs]

20A. When a lease includes both land and buildings elements, an entity assesses the classification of each element as a finance or an operating lease separately in accordance with paragraphs 12–18. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.

21. Whenever necessary in order to classify and account for a lease of land and buildings, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the buildings elements in proportion to the relative fair values of the leasehold interests in the land element and buildings element of the lease at the inception of the lease. If the lease payments cannot be allocated reliably between these two elements, the entire lease is classified as a finance lease, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.

22. For a lease of land and buildings in which the amount that would initially be recognized for the land element, in accordance with paragraph 28, is immaterial, the land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease in accordance with paragraphs 12–18. In such a case, the economic life of the buildings is regarded as the economic life of the entire leased asset.

23. Separate measurement of the land and buildings elements is not required when the lessee's interest in both land and buildings is classified as an investment property in accordance with SLPSAS 13, and the fair value model is adopted. Detailed calculations are required for this assessment only if the classification of one or both elements is otherwise uncertain.

24. In accordance with SLPSAS 13, it is possible for a lessee to classify a property interest held under an operating lease as an investment property. If it does, the property interest is accounted for as if it were a finance lease and, in addition, the fair value model is used for the asset recognized. The lessee shall continue to account for the lease as a finance lease, even if a subsequent event changes the nature of the lessee's property interest so that it is no longer classified as investment property. This will be the case if, for example, the lessee:

(a) Occupies the property, which is then transferred to owner-occupied property at a deemed cost equal to its fair value at the date of change in use; or

(b) Grants a sublease that transfers substantially all of the risks and rewards incidental to ownership of the interest to an unrelated third party. Such a sublease is accounted for by the lessee as a finance lease to the third party, although it may be accounted for as an operating lease by the third party.

Leases and Other Contracts

25. A contract may consist solely of an agreement to lease an asset. However, a lease may also be one element in a broader set of agreements with private sector entities to construct, own, operate, and/or transfer assets. Public

sector entities often enter into such agreements, particularly in relation to long-lived physical assets and infrastructure assets. Other agreements may involve a public sector entity leasing infrastructure from the private sector.

26. Where an arrangement contains an identifiable operating lease or finance lease as defined in this Standard, the provisions of this Standard are applied in accounting for the lease component of the arrangement.

27. Public sector entities may also enter a variety of agreements for the provision of goods and/or services, which necessarily involve the use of dedicated assets. In some of these agreements, it may not be clear whether or not a lease, as defined by this Standard, has arisen. In these cases, professional judgment is exercised, and if a lease has arisen this standard is applied; if a lease has not arisen, entities account for those agreements by applying the provisions of other relevant SLPSASs, or in the absence thereof, other relevant international and/or national accounting standards.

Leases in the Financial Statements of Lessees

Finance Leases

28. **At the commencement of the lease term, lessees shall recognize assets acquired under finance leases as assets, and the associated lease obligations as liabilities in their statements of financial position. The assets and liabilities shall be recognized at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used.**

29. Transactions and other events are accounted for and presented in accordance with their substance and financial reality, and not merely with legal form. Although the legal form of a lease agreement is that the lessee may acquire no legal title to the leased asset, in the case of finance leases the substance and financial reality are that the lessee acquires the economic benefits or service potential of the use of the leased asset for the major part of its economic life in return for entering into an obligation to pay for that right an amount approximating, at the inception of the lease, the fair value of the asset and the related finance charge.

30. If such lease transactions are not reflected in the lessee's financial statements, the assets and liabilities of an entity are understated, thereby distorting financial ratios. Therefore, it is appropriate for a finance lease to be recognized in the lessee's financial statements both as an asset and as an obligation to pay future lease payments. At the commencement of the lease term, the asset and the liability for the future lease payments are recognized in the financial statements at the same amounts, except for any initial direct costs of the lessee that are added to the amount recognized as an asset.

31. It is not appropriate for the liabilities for leased assets to be presented in the financial statements as a deduction from the leased assets.

32. If, for the presentation of liabilities on the face of the statement of financial position, a distinction is made between current and non-current liabilities, the same distinction is made for lease liabilities.

33. Initial direct costs are often incurred in connection with specific leasing activities, such as negotiating and securing leasing arrangements. The costs identified as directly attributable to activities performed by the lessee for a finance lease are added to the amount recognized as an asset.

34. **Minimum lease payments shall be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge shall be allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents shall be charged as expenses in the period in which they are incurred.**

35. In practice, in allocating the finance charge to periods during the lease term, a lessee may use some form of approximation to simplify the calculation.

36. **A finance lease gives rise to a depreciation expense for depreciable assets as well as a finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognized shall be calculated in accordance with SLPSAS 7, Property, Plant, and Equipment, and SLPSAS 20, Intangible Assets, as appropriate. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term or its useful life**.

37. The depreciable amount of a leased asset is allocated to each accounting period during the period of expected use on a systematic basis consistent with the depreciation policy the lessee adopts for depreciable assets that are owned. If there is reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise the asset is depreciated over the shorter of the lease term or its useful life.

38. The sum of the depreciation expense for the asset and the finance expense for the period is rarely the same as the lease payments payable for the period, and it is therefore inappropriate simply to recognize the lease payments payable as an expense. Accordingly, the asset and the related liability are unlikely to be equal in amount after the commencement of the lease term.

39. To determine whether a leased asset has become impaired, an entity applies relevant impairment tests in international and/or national accounting standards.

40. **Lessees shall disclose the following for finance leases:**

  (a) **For each class of asset, the net carrying amount at the reporting date;**

  (b) **A reconciliation between the total of future minimum lease payments at the reporting date, and their present value;**

  (c) **In addition, an entity shall disclose the total of future minimum lease payments at the reporting date, and their present value, for each of the following periods:**

    (i) **Not later than one year;**

    (ii) **Later than one year and not later than five years; and**

    (iii) **Later than five years;**

  (d) **Contingent rents recognized as an expense in the period;**

  (e) **The total of future minimum sublease payments expected to be received under non-cancelable subleases at the reporting date; and**

  (f) **A general description of the lessee's material leasing arrangements including, but not limited to, the following:**

    (i) **The basis on which contingent rent payable is determined;**

    (ii) **The existence and terms of renewal or purchase options and escalation clauses; and**

    (iii) **Restrictions imposed by lease arrangements, such as those concerning return of surplus, return of capital contributions, dividends or similar distributions, additional debt, and further leasing.**

41. In addition, the requirements for disclosure in accordance with SLPSAS 13, SLPSAS 7, and SLPSAS 20, that have been adopted by the entity are applied to the amounts of leased assets under finance leases that are accounted for by the lessee as acquisitions of assets.

Operating Leases

42. **Lease payments under an operating lease shall be recognized as an expense on a straight-line basis over the lease term, unless another systematic basis is representative of the time pattern of the user's benefit.**

43. For operating leases, lease payments (excluding costs for services such as insurance and maintenance) are recognized as an expense on a straight-line basis, unless another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis.

44. **Lessees shall disclose the following for operating leases:**

(a) **The total of future minimum lease payments under noncancelable operating leases for each of the following periods:**

(i) **Not later than one year;**

(ii) **Later than one year and not later than five years; and**

(iii) **Later than five years;**

(b) **The total of future minimum sublease payments expected to be received under non-cancelable subleases at the reporting date;**

(c) **Lease and sublease payments recognized as an expense in the period, with separate amounts for minimum lease payments, contingent rents, and sublease payments; and**

(d) **A general description of the lessee's significant leasing arrange ments including, but not limited to, the following:**

   (i) **The basis on which contingent rent payments are determined;**

   (ii) **The existence and terms of renewal or purchase options and escalation clauses; and**

   (iii) **Restrictions imposed by lease arrangements, such as those concern ing return of surplus, return of capital contri butions, dividends or simi lar distributions, additional debt, and further leasing.**

Leases in the Financial Statements of Lessors

Finance Leases

45. This Standard describes the treatment of finance revenue earned under finance leases. The term "manufacturer or trader lessor" is used in this Standard to refer to all public sector entities that manufacture or trade assets and also act as lessors of those assets, regardless of the scale of their leasing, trading, and manufacturing activities. With respect to an entity that is a manufacturer or trader lessor, the Standard also describes the treatment of gains or losses arising from the transfer of assets.

46. Public sector entities may enter into finance leases as a lessor under a variety of circumstances. Some public sector entities may trade assets on a regular basis. For example, governments may create special purpose entities that are responsible for the central procurement of assets and supplies for all other entities. Centralization of the purchasing function may provide greater opportunity to obtain trade discounts or other favorable conditions. In some jurisdictions, a central purchasing entity may purchase items on behalf of other entities, with all transactions being conducted in the name

of the other entities. In other jurisdictions, a central purchasing entity may purchase items in its own name, and its functions may include:

(a) Procuring assets and supplies;

(b) Transferring assets by way of sale or finance lease; and/or

(c) Managing a portfolio of assets, such as a motor vehicle fleet, for use by other entities, and making those assets available for short or long-term lease, or purchase.

47. Other public sector entities may enter into lease transactions on a more limited scale and at less frequent intervals. In particular, in some jurisdictions public sector entities that have traditionally owned and operated infrastructure assets such as roads, dams, and water treatment plants are no longer automatically assuming complete ownership and operational responsibility for these assets. Public sector entities may transfer existing infrastructure assets to private sector entities by way of sale or by way of finance lease. In addition, public sector entities may construct new long-lived physical and infrastructure assets in partnership with private sector entities, with the intention that the private sector entity will assume responsibility for the assets by way of outright purchase or by way of finance lease once they are completed. In some cases, the arrangement provides for a period of control by the private sector before reversion of title and control of the asset to the public sector – for example, a local government may build a hospital and lease the facility to a private sector company for a period of twenty years, after which time the facility reverts to public control.

48. **Lessors shall recognize lease payments receivable under a finance lease as assets in their statements of financial position. They shall present such assets as a receivable at an amount equal to the net investment in the lease.**

49. Under a finance lease, substantially all the risks and rewards incidental to legal ownership are transferred by the lessor, and thus the lease payment receivable is treated by the lessor as repayment of principal and finance revenue to reimburse and reward the lessor for its investment and services.

Initial Recognition

50. Initial direct costs are often incurred by lessors, and include amounts such as commissions, legal fees, and internal costs that are incremental and directly attributable to negotiating and arranging a lease. They exclude general overheads, such as those incurred by a sales and marketing team. For finance leases other than those involving manufacturer or trader lessors, initial direct costs are included in the initial measurement of the finance lease receivable, and reduce the amount of revenue recognized over the lease term. The interest rate implicit in the lease is defined in such a way that the initial direct costs are included automatically in the finance lease receivable; there is no need to add them separately. Costs incurred by manufacturer or trader lessors in connection with negotiating and arranging a lease are excluded

from the definition of initial direct costs. As a result, they are excluded from the net investment in the lease, and are recognized as an expense when the gain or loss on sale is recognized, which for a finance lease is normally at the commencement of the lease term.

51. **The recognition of finance revenue shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.**

52. A lessor aims to allocate finance revenue over the lease term on a systematic and rational basis. This revenue allocation is based on a pattern reflecting a constant periodic return on the lessor's net investment in the finance lease. Lease payments relating to the accounting period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance revenue.

53. Estimated unguaranteed residual values used in computing the lessor's gross investment in a lease are reviewed regularly. If there has been a reduction in the estimated unguaranteed residual value, the revenue allocation over the lease term is revised, and any reduction in respect of amounts already accrued is recognized immediately.

54. **Manufacturer or trader lessors shall recognize gains or losses on sale of assets in the period, in accordance with the policy followed by the entity for outright sales.**

55. **If artificially low rates of interest are quoted, any gains or losses on sale of assets shall be restricted to what would apply if a market rate of interest were charged. Costs incurred by manufacturer or trader lessors in connection with negotiating and arranging a lease shall be recognized as an expense when the gain or loss is recognized.**

56. Public sector entities that manufacture or trade assets may offer to potential purchasers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or trader lessor gives rise to two types of revenue:

    (a) The gain or loss equivalent to the gain or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and

    (b) The finance revenue over the lease term.

57. The sales revenue recognized at the commencement of the lease term by a manufacturer or trader lessor is the fair value of the asset or, if lower, the present value of the minimum lease payments accruing to the lessor, computed at a commercial rate of interest. The cost of sale of an asset recognized at the commencement of the lease term is the cost, or carrying amount if different, of the leased property, less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the gain or loss on sale that is recognized in accordance with the entity's policy for outright sales.

58. Manufacturer or trader lessors may sometimes offer customers lower rates of interest than their normal lending rates. The use of such a rate would result in an excessive portion of the total revenue from the transaction being recognized at the time of sale. If artificially low rates of interest are quoted, revenue recognized as gain or loss on sale is restricted to what would apply if the entity's normal lending rate for that type of transaction were charged.

59. Initial direct costs are recognized as an expense at the commencement of the lease term because they are mainly related to earning the manufacturer's or trader's gain or loss on sale.

60. **Lessors shall disclose the following for finance leases:**

(a) **A reconciliation between the total gross investment in the lease at the reporting date, and the present value of minimum lease payments receivable at the reporting date. In addition, an entity shall disclose the gross investment in the lease and the present value of minimum lease payments receivable at the reporting date, for each of the following periods:**

(i) **Not later than one year;**

(ii) **Later than one year and not later than five years; and**

(iii) **Later than five years;**

(b) **Unearned finance revenue;**

(c) **The unguaranteed residual values accruing to the benefit of the lessor;**

(d) **The accumulated allowance for uncollectible minimum lease payments receivable;**

(e) **Contingent rents recognized in the statement of financial performance; and**

(f) **A general description of the lessor's material leasing arrangements.**

61. As an indicator of growth in leasing activities, it is often useful to also disclose the gross investment less unearned revenue in new business added during the accounting period, after deducting the relevant amounts for canceled leases.

Operating Leases

62. **Lessors shall present assets subject to operating leases in their statements of financial position according to the nature of the asset.**

63. **Lease revenue from operating leases shall be recognized as revenue on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which benefits derived from the leased asset is diminished.**

64. Costs, including depreciation, incurred in earning the lease revenue are recognized as an expense. Lease revenue (excluding receipts for services provided, such as insurance and maintenance) is recognized as revenue on a straight-line basis over the lease term, even if the receipts are not on such a basis, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.

65. **Initial direct costs incurred by lessors in negotiating and arranging an operating lease shall be added to the carrying amount of the leased asset, and recognized as an expense over the lease term on the same basis as the lease revenue.**

66. **The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets, and depreciation shall be calculated in accordance with SLPSAS 7 or SLPSAS 20, as appropriate.**

67. To determine whether a leased asset has become impaired, an entity applies relevant impairment tests in international and/or national accounting standards.

68. A manufacturer or trader lessor does not recognize any gain on sale on entering into an operating lease because it is not the equivalent of a sale.

69. **Lessors shall disclose the following for operating leases:**

(a) **The future minimum lease payments under non-cancelable operating leases in the aggregate and for each of the following periods:**

(i) **Not later than one year;**

(ii) **Later than one year and not later than five years; and**

(iii) **Later than five years;**

(b) **Total contingent rents recognized in the statement of financial performance in the period; and**

(c) **A general description of the lessor's leasing arrangements.**

Sale and Leaseback Transactions

70. A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent, because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.

71 **If a sale and leaseback transaction results in a finance lease, any excess of sales proceeds over the carrying amount shall not be immediately recognized as revenue by a seller-lessee. Instead, it shall be deferred and amortized over the lease term.**

72. If the leaseback is a finance lease, the transaction is a means whereby the lessor provides finance to the lessee, with the asset as security. For this reason, it is not appropriate to regard an excess of sales proceeds over the carrying amount as revenue. Such excess is deferred and amortized over the lease term.

73. **If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, any gain or loss shall be recognized immediately. If the sale price is below fair value, any gain or loss shall be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it shall be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value shall be deferred and amortized over the period for which the asset is expected to be used.**

74. If the leaseback is an operating lease, and the lease payments and the sale price are at fair value, there has in effect been a normal sale transaction and any gain or loss is recognized immediately.

75, **For operating leases, if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset, a loss equal to the amount of the difference between the carrying amount and fair value shall be recognized immediately.**

76. For finance leases, no such adjustment is necessary unless (a) there has been an impairment in value, and (b) that impairment is required to be recognized by any international and/or national accounting standard on impairment that has been adopted by the entity.

77. Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of the material leasing arrangements leads to disclosure of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

78. Sale and leaseback transactions may be required to be separately disclosed in accordance with SLPSAS 1.

Transitional Provisions

79. **All provisions of this Standard shall be applied from the date of first adoption of accrual accounting in accordance with SLPSASs, except in relation to leased assets that have not been recognized as a result of transitional provisions under another SLPSAS. The provisions of this Standard would not be required to apply to such assets until the transitional provision in the other IPSAS expires. In no case shall the existence of transitional provisions in other Standards preclude the full application of accrual accounting in accordance with SLPSASs.**

80. Notwithstanding the existence of transitional provisions under another SLPSAS, entities that are in the process of adopting the accrual basis of

accounting are encouraged to comply in full with the provisions of that other standard as soon as possible.

81. **Subject to paragraph 83, retrospective application of this Standard by entities that have already adopted the accrual basis of accounting and that intend to comply with SLPSASs as they are issued is encouraged but not required. If the Standard is not applied retrospectively, the balance of any pre-existing finance lease is deemed to have been properly determined by the lessor, and shall be accounted for thereafter in accordance with the provisions of this Standard.**

82. Entities that have already adopted the accrual basis of accounting, and that intend to comply with SLPSASs as they are issued, may have pre-existing finance leases that have been recognized as assets and liabilities in the statement of financial position. Retrospective application of this Standard to existing finance leases is encouraged. Retrospective application could lead to the restatement of such assets and liabilities. Such assets and liabilities are required to be restated only if the Standard is applied retrospectively.

83. [Not used to maintain consistency of paragraph numbers with IPSASs]

84. [Not used to maintain consistency of paragraph numbers with IPSASs]

Effective Date

85. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1, 2018. Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1, 2018. it shall disclose that fact.**

86. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Implementation Guidance

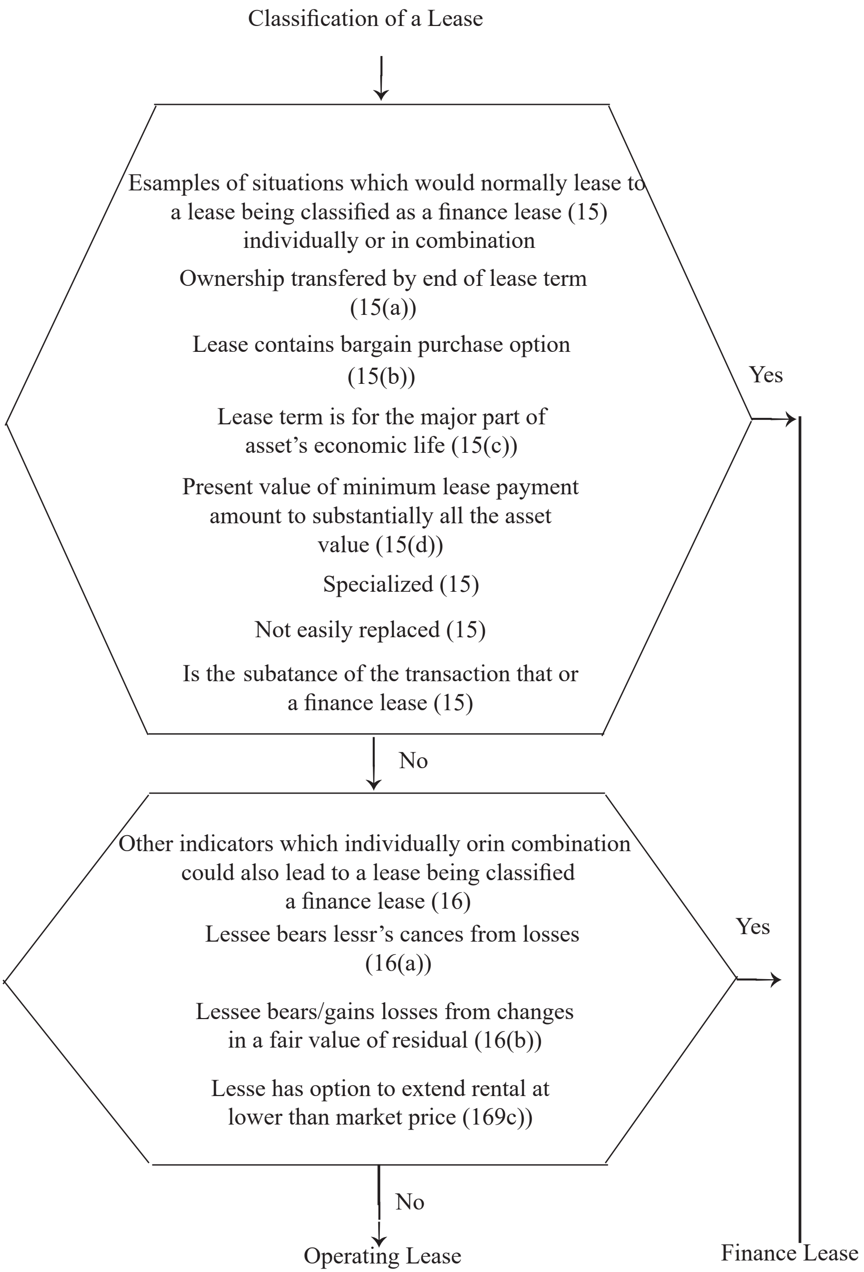
This guidance accompanies, but is not part of, SLPSAS 12.

Classification of a Lease

IG1. The objective of the chart on the next page is to assist in classifying a lease as either a finance lease or an operating lease. A finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset. An operating lease is a lease other than a finance lease.

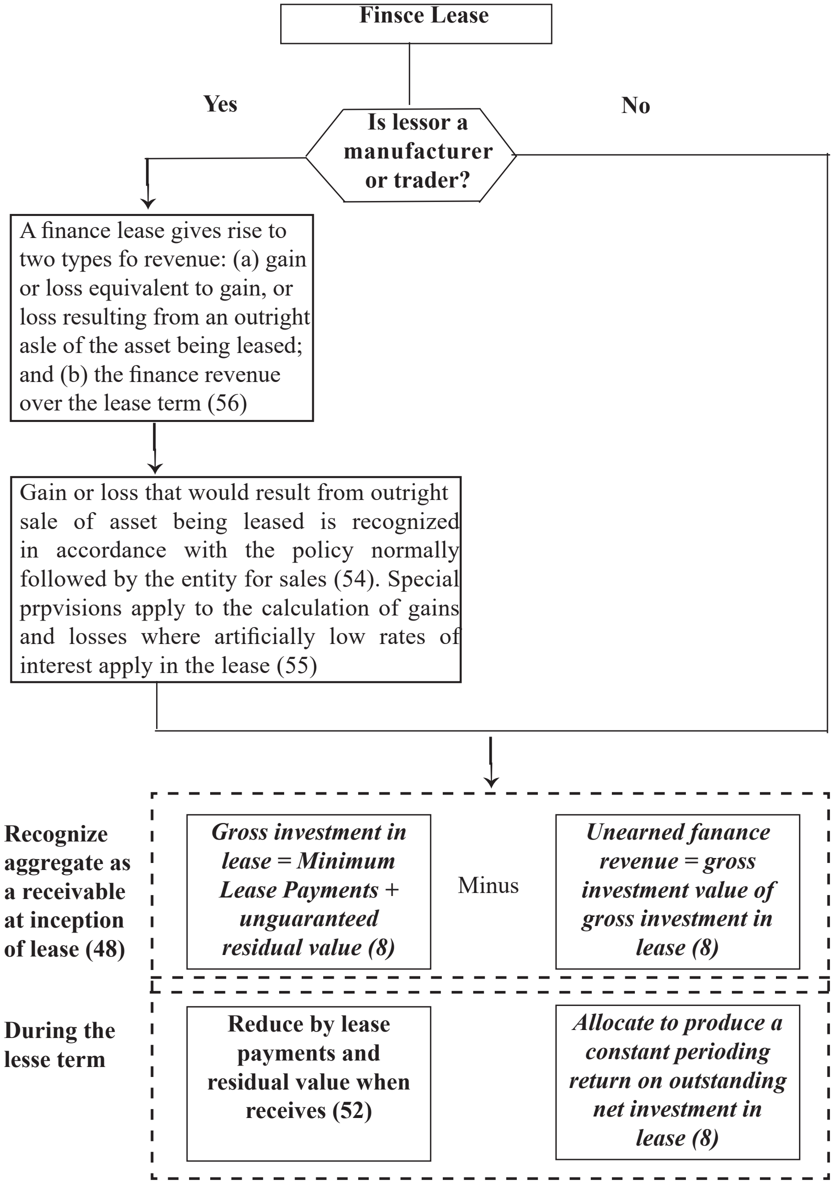
IG2. The examples contained in this chart do not necessarily reflect all possible situations in which a lease may be classified as a finance lease, nor should a lease necessarily be classified as a finance lease by virtue of the route followed in this chart. Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract (paragraph 15).

IG3. In the flowchart, the numbers in parentheses refer to paragraph numbers in this Standard.


Classification of a Lease
Esamples of situations which would normally lease to a lease being classified as a finance lease (15) individually or in combination
Ownership transfered by end of lease term (15(a))
Lease contains bargain purchase option (15(b))
Lease term is for the major part of asset's economic life (15(c))
Present value of minimum lease payment amount to substantially all the asset value (15(d))
Specialized (15)
Not easily replaced (15)
Is the subatance of the transaction that or a finance lease (15)
Yes
No
Other indicators which individually orin combination could also lead to a lease being classified a finance lease (16)
Lessee bears lessr's cances from losses (16(a))
Lessee bears/gains losses from changes in a fair value of residual (16(b))
Lesse has option to extend rental at lower than market price (169c))
Yes
No
Operating Lease
Finance Lease

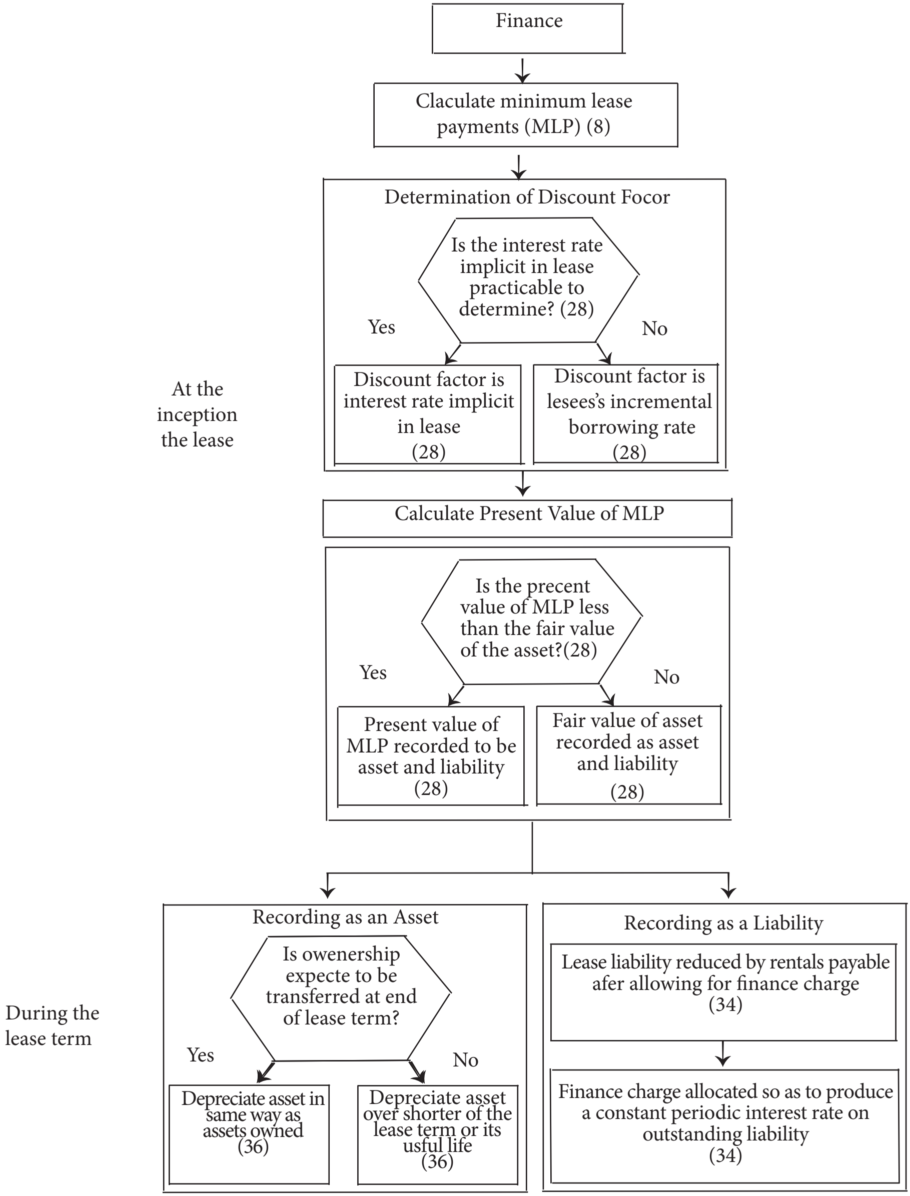
Accounting for a Finance Lease by a Lessor

IG4. In the flowchart, the numbers in parentheses refer to paragraph numbers in the Standard.



Accounting for a Finance Lease by a Lessee

IG5. In the flowchart, the numbers in parentheses refer to paragraph numbers in the Standard.



Sale and Leaseback Transactions that Result in Operating Leases

IG6. A sale and leaseback transaction that results in an operating lease may give rise to a gain or a loss, the determination and treatment of which depends upon the leased asset's carrying amount, fair value, and selling price. The table on the following page shows the requirements of this Standard in various circumstances.

Sale price established at fair value (parsgaraph 65)	**Carrying amount equal to fair value**	**Carring amount less than fair value**	**Carrring amount abovw fair value**
Gain	no gain	recognize gain immediately	no gain
Loss	no loss	no loss	recognize loss immediately

Sale price below fair value (paragraph)	**Carring amount equal to fair value**	**Carring amount less than fair value**	**Carring amount above fair value**
Gain	no gain	recognize gain immediately	no gain (note 1)
Loss not compensated by future lease payments at below market price	recognize loss immediately	recognize loss immediately	(note 1)
Loss compensated by future lease payments at below market price	defer and amortize loss	defer and amortize loss	(note 1)

Sale price above fair value *(paragraph 65)*	**Carrying amount equal to fair value**	**Carrying amount less than fair value**	**Carrying amount above fair value**
Gain	defer and amortize gain	defer and amortize gain (note 2)	defer and amortize gain (note 3)
Loss	No loss	No loss	(note 1)

Note 1 These parts of the table represent circumstances that would have been dealt with under paragraph 75 of this Standard. Paragraph 75 requires the carrying amount of an asset to be written down to fair value where it is subject to a sale and leaseback.

Note 2 If the sale price is above fair value, the excess over fair value should be deferred and amortized over the period for which the asset is expected to be used (paragraph 73).

Note 3 The gain would be the difference between fair value and sale price, as the carrying amount would have been written down to fair value in accordance with paragraph 75.

Calculating the Interest Rate Implicit in a Finance Lease

IG7. The Standard (paragraph 28) requires the lessees of assets acquired under finance leases to calculate the interest rate implicit in a lease, where practical. Paragraph 34 requires the lessees to apportion lease payments between the finance charge and the reduction of the outstanding liability, using the interest rate implicit in the lease. Many lease agreements explicitly identify the interest rate implicit in the lease, but some do not. If a lease agreement does not identify the interest rate implicit in the lease the lessee needs to calculate the rate, using the present value formula. Financial calculators and spreadsheets will automatically calculate the interest rate implicit in a lease. Where these are not available, entities can use the present value formula to manually calculate the rate. This guidance illustrates the following two common methods for calculating the interest rate: trial and error, and interpolation. Both methods use the present value formula to derive the interest rate.

IG8. Derivations of present value formulas are widely available in accounting and finance textbooks. The present value (PV) of minimum lease payments (MLP) is calculated by means of the following formula:

$$PV(MLP) = \frac{S}{(1+r)^n} + \frac{A}{r}\left[1 - \frac{1}{(1+r)^n}\right]$$

Where:

“S” is the guaranteed residual value

“A” is the regular periodical payment

“r” is the periodic interest rate implicit in the lease expressed as a decimal

“n” is the number of periods in the term of the lease

Example

IG8. Department X enters into an agreement to acquire a motor vehicle on a finance lease. The fair value of the motor vehicle at the inception of the lease is 25,000 rupees; the annual lease payments are 5,429 rupees payable in arrears; the lease term is four years; and the guaranteed residual value is 10,000 rupees. The lease agreement does not provide for any services additional to the supply of the motor vehicle. Department X is responsible for all the running costs of the vehicle, including insurance, fuel, and maintenance. The lease agreement does not specify the interest rate implicit in the lease. The Department’s incremental borrowing rate is 7% per annum. Several financial institutions are advertising loans secured by motor vehicles at rates varying between 7.5% and 10%.

IG9. The calculation is an iterative process – that is, the lessee must make a “best guess” of the interest rate and calculate the present value of the minimum lease payments and compare the result to the fair value of the leased asset at the inception of the lease. If the result is less than the fair value, the interest rate selected was too high; if the result is greater than the fair value, the interest rate selected was too low. The interest rate implicit in a lease is the rate used when the present value of the minimum lease payments is equal to the fair value of the leased asset at the inception of the lease.

IG10. Department X would begin calculations using a best estimate – for example its incremental borrowing rate of 7% per annum, which is too low. It would then use the maximum feasible rate – for example the 10% per annum rate offered for loans secured by a motor vehicle, which would prove too high. After several calculations, it would arrive at the correct rate of 8.5% per annum.

IG11. To calculate the interest rate, the Department uses the PV(MLP) formula above, where:

S = 10,000 n = 4 r = Annual interest rate expressed as a decimal

A = 5,429 Target PV(MLP) = 25,000

IG12. At Department X's incremental borrowing rate of 7% (0.07) per annum (figures are rounded):

$$\text{PV(MLP)} = \frac{10,000}{(1+0.07)^4} + \frac{5,429}{0.07}\left[1 - \frac{1}{(1+0,07)^4}\right]$$

= 7,629 + 18,390

= 26,019

IG13. The PV(MLP) using the incremental borrowing rate is greater than the fair value of the leased asset, therefore a higher rate is implicit in the lease. The Department must make calculations at other rates to determine the actual rate (figures are rounded):

PV(MLP) at 7.5%	= 25,673	Interest rate too low
PV(MLP) at 10%	= 24,040	Interest rate too high
PV(MLP) at 9%	= 24,674	Interest rate too high
PV(MLP) at 8%	= 25,333	Interest rate too low
PV(MLP) at 8.5%	= 25,000	Correct interest rate

IG14. The Department will now use the interest rate of 8.5% to apportion the lease payments between the finance charge and the reduction of the lease liability, as shown in the table below.

Interpolation Method

Apportionment of Lease payment (figures are rounded)

IG15. Calculating the interest rate implicit in a lease requires lessees to initially calculate the present value for an interest rate that is too high, and one that is too low. The differences (in absolute terms) between the results obtained and the actual net present value are used to interpolate the correct interest rate. Using the data provided above, and the results for 7% and 10%, the actual rate can be interpolated as follows (figures are rounded): PV at 7% = 26,019, difference = 1,019 (i.e., 26,019 – 25,000)

PV at 10% = 24,040, difference = 960 (i.e., 24,040 – 25,000)

$$r = 7\% + (10\% - 7\%)\ \frac{1,019}{(1,019 + 960)}$$

$$= 7\% + (3\% \times 0.5\%)$$
$$= 7\% + 1.5\%$$
$$= 8.5\%$$

IG16. Department X will now use the interest rate of 8.5% to record the lease in its books and apportion the lease payments between the finance charge and the reduction of the lease liability, as shown in the table below.

	Year 0	**Year 1**	**Year 2**	**Year 3**	**Year 4**
Opening PV of Lease Liability	25,000	25,000	21,696	18,110	14,221
Interest Expense	–	2,125	1,844	1,539	1,209
Reduction of Liability	–	3,304	3,585	3,890	14,221*
Closing Lease Liability	25,000	21,696	18,110	14,221	–

* Includes payment of guaranteed residual value.

SLPSAS – 13- Investment Properties
Acknowledgement

Investment Properties (SLPSAS – 13) of the “Sri Lanka Public Sector Accounting Standards – Volume III” is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 13 - INVESTMENT PROPERTY
CONTENTS

Sri Lanka Public Sector Accounting Standard 16, Investment Property, is set out in paragraphs 1–102. All the paragraphs have equal authority. SLPSAS 13 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.

Socope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for investment property.**

3. This Standard applies to all public sector entities other than Government Business Enterprises.

4. The Preface to Sri Lanka Public Sector Accounting Standards issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, Presentation of Financial Statements.

5. This Standard applies to accounting for investment property, including (a) the measurement in a lessee's financial statements of investment property interests held under a lease accounted for as a finance lease, and to (b) the measurement in a lessor's financial statements of investment property provided to a lessee under an operating lease. This Standard does not deal with matters covered in SLPSAS 12, Leases, including:

   (a) Classification of leases as finance leases or operating leases;

   (b) Recognition of lease revenue from investment property (see also SLPSAS 10, Revenue from Exchange Transactions);

   (c) Measurement in a lessee's financial statements of property interests held under a lease accounted for as an operating lease;

   (d) Measurement in a lessor's financial statements of its net investment in a finance lease;

   (e) Accounting for sale and leaseback transactions; and

   (f) Disclosure about finance leases and operating leases.

6.This Standard does not apply to:

   (a) Biological assets related to agricultural activity; and

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

Definitions

7. **The following terms are used in this Standard with the meanings specified:**

Carrying amount (for the purpose of this Standard) is the amount at which an asset is recognized in the statement of financial position.

Cost is the amount of cash or cash equivalents paid or the fair value of other consideration given to acquire an asset at the time of its acquisition or construction.

Investment property is property (land or a building – or part of a building – or both) held to earn rentals or for capital appreciation, or both, rather than for:

(a) **Use in the production or supply of goods or services, for administrative purposes; or**

(b) **Sale in the ordinary course of operations.**

Owner-occupied property is property held (by the owner or by the lessee under a finance lease) for use in the production or supply of goods or services, or for administrative purposes.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of *Defined Terms* published separately.

Property Interest Held by a Lessee under an Operating Lease

8. A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property if, and only if, (a) the property would otherwise meet the definition of an investment property, and (b) the lessee uses the fair value model set out in paragraphs 42–64 for the asset recognized. This classification alternative is available on a property-by-property basis. However, once this classification alternative is selected for one such property interest held under an operating lease, all property classified as investment property shall be accounted for using the fair value model. When this classification alternative is selected, any interest so classified is included in the disclosures required by paragraphs 85–89.

Investment Property

9. There are a number of circumstances in which public sector entities may hold property to earn rental and for capital appreciation. For example, a public sector entity (other than a GBE) may be established to manage a government's property portfolio on a commercial basis. In this case, the property held by the entity, other than property held for resale in the ordinary course of operations, meets the definition of an investment

property. Other public sector entities may also hold property for rentals or capital appreciation, and use the cash generated to finance their other (service delivery) activities. For example, a university or local government may own a building for the purpose of leasing on a commercial basis to external parties to generate funds, rather than to produce or supply goods and services. This property would also meet the definition of investment property.

10. Investment property is held to earn rentals or for capital appreciation, or both. Therefore, investment property generates cash flows largely independently of the other assets held by an entity. This distinguishes investment property from other land or buildings controlled by public sector entities, including owner-occupied property. The production or supply of goods or services (or the use of property for administrative purposes) can also generate cash flows. For example, public sector entities may use a building to provide goods and services to recipients in return for full or partial cost recovery. However, the building is held to facilitate the production of goods and services, and the cash flows are attributable not only to the building, but also to other assets used in the production or supply process. SLPSAS 7, Property, Plant, and Equipment, applies to owner-occupied property.

11. In some public sector jurisdictions, certain administrative arrangements exist such that an entity may control an asset that may be legally owned by another entity. For example, a government department may control and account for certain buildings that are legally owned by the State. In such circumstances, references to owner-occupied property means property occupied by the entity that recognizes the property in its financial statements.

12. The following are examples of investment property:

    (a) Land held for long-term capital appreciation rather than for short-term sale in the ordinary course of operations. For example, land held by a hospital for capital appreciation that may be sold at a beneficial time in the future.

    (b) Land held for a currently undetermined future use. (If an entity has not determined that it will use the land as owner-occupied property, including occupation to provide services such as those provided by national parks to current and future generations, or for short-term sale in the ordinary course of operations, the land is regarded as held for capital appreciation).

    (c) A building owned by the entity (or held by the entity under a finance lease) and leased out under one or more operating leases on a commercial basis. For example, a university may own a building that it leases on a commercial basis to external parties.

    (d) A building that is vacant but is held to be leased out under one or more operating leases on a commercial basis to external parties.

(e) Property that is being constructed or developed for future use as investment property.

13. The following are examples of items that are not investment property and are therefore outside the scope of this Standard:

(a) Property held for sale in the ordinary course of operations or in the process of construction or development for such sale (see SLPSAS 9, Inventories). For example, a municipal government may routinely supplement rate income by buying and selling property, in which case property held exclusively with a view to subsequent disposal in the near future or for development for resale is classified as inventory. A housing department may routinely sell part of its housing stock in the ordinary course of its operations as a result of changing demographics, in which case any housing stock held for sale is classified as inventory.

(b) Property being constructed or developed on behalf of third parties. For example, a property and service department may enter into construction contracts with entities external to its government (see SLPSAS 16, Construction Contracts).

(c) Owner-occupied property (see SLPSAS 7), including (among other things) property held for future use as owner-occupied property, property held for future development and subsequent use as owner-occupied property, property occupied by employees such as housing for military personnel (whether or not the employees pay rent at market rates) and owner-occupied property awaiting disposal.

(d) [Not used to maintain consistency of sub-paragraph numbers with IPSASs]

(e) Property that is leased to another entity under a finance lease.

(f) Property held to provide a social service and which also generates cash inflows. For example, a housing department may hold a large housing stock used to provide housing to low income families at below market rental. In this situation, the property is held to provide housing services rather than for rentals or capital appreciation and rental revenue generated is incidental to the purposes for which the property is held. Such property is not considered an "investment property" and would be accounted for in accordance with SLPSAS 7.

(g) Property held for strategic purposes which would be accounted for in accordance with SLPSAS 7.

14. In many jurisdictions, public sector entities will hold property to meet service delivery objectives rather than to earn rental or for capital appreciation. In such situations, the property will not meet the definition of investment property. However, where a public sector entity does hold property to

earn rental or for capital appreciation, this Standard is applicable. In some cases, public sector entities hold some property that comprises (a) a portion that is held to earn rentals or for capital appreciation rather than to provide services, and (b) another portion that is held for use in the production or supply of goods or services or for administrative purposes. For example, a hospital or a university may own a building, part of which is used for administrative purposes, and part of which is leased out as apartments on a commercial basis. If these portions could be sold separately (or leased out separately under a finance lease), an entity accounts for the portions separately. If the portions could not be sold separately, the property is investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.

15. In some cases, an entity provides ancillary services to the occupants of a property it holds. An entity treats such a property as investment property if the services are insignificant to the arrangement as a whole. An example is when a government agency (a) owns an office building that is held exclusively for rental purposes and rented on a commercial basis, and (b) also provides security and maintenance services to the lessees who occupy the building.

16. In other cases, the services provided are significant. For example, a government may own a hotel or hostel that it manages through its general property management agency. The services provided to guests are significant to the arrangement as a whole. Therefore, an owner-managed hotel or hostel is owner-occupied property, rather than investment property.

17. It may be difficult to determine whether ancillary services are so significant that a property does not qualify as investment property. For example, a government or government agency that is the owner of a hotel may transfer some responsibilities to third parties under a management contract. The terms of such management contracts vary widely. At one end of the spectrum, the government's or government agency's position may, in substance, be that of a passive investor. At the other end of the spectrum, the government or government agency may simply have outsourced day-to-day functions, while retaining significant exposure to variation in the cash flows generated by the operations of the hotel.

18. Judgment is needed to determine whether a property qualifies as investment property. An entity develops criteria so that it can exercise that judgment consistently in accordance with the definition of investment property, and with the related guidance in paragraphs 9–17. Paragraph 86(c) requires an entity to disclose these criteria when classification is difficult.

19. In some cases, an entity owns property that is leased to, and occupied by, its controlling entity or another controlled entity. The property does not qualify as investment property in consolidated financial statements, because the property is owner-occupied from the perspective of the economic entity.

However, from the perspective of the entity that owns it, the property is investment property if it meets the definition in paragraph 7. Therefore, the lessor treats the property as investment property in its individual financial statements. This situation may arise where a government establishes a property management entity to manage government office buildings. The buildings are then leased out to other government entities on a commercial basis. In the financial statements of the property management entity, the property would be accounted for as investment property. However, in the consolidated financial statements of the government, the property would be accounted for as property, plant, and equipment in accordance with SLPSAS 7.

Recognition

20. **Investment property shall be recognized as an asset when, and only when:**

    (a) **It is probable that the future economic benefits or service potential that are associated with the investment property will flow to the entity; and**

    (b) **The cost or fair value of the investment property can be measured reliably.**

21. In determining whether an item satisfies the first criterion for recognition, an entity needs to assess the degree of certainty attaching to the flow of future economic benefits or service potential on the basis of the available evidence at the time of initial recognition. Existence of sufficient certainty that the future economic benefits or service potential will flow to the entity necessitates an assurance that the entity will receive the rewards attaching to the asset, and will undertake the associated risks. This assurance is usually only available when the risks and rewards have passed to the entity. Before this occurs, the transaction to acquire the asset can usually be cancelled without significant penalty and, therefore, the asset is not recognized.

22. The second criterion for recognition is usually readily satisfied because the exchange transaction evidencing the purchase of the asset identifies its cost. As specified in paragraph 27 of this Standard, under certain circumstances an investment property may be acquired at no cost or for a nominal cost. In such cases, cost is the investment property's fair value as at the date of acquisition.

23. An entity evaluates under this recognition principle all its investment property costs at the time they are incurred. These costs include costs incurred initially to acquire an investment property, and costs incurred subsequently to add to, replace part of, or service a property.

24. Under the recognition principle in paragraph 20, an entity does not recognize in the carrying amount of an investment property the costs of the day-to-day servicing of such a property. Rather, these costs are recognized in surplus or deficit as incurred. Costs of day-to-day servicing

are primarily the costs of labor and consumables, and may include the cost of minor parts. The purpose of these expenditures is often described as for the repairs and maintenance of the property.

25. Parts of investment property may have been acquired through replacement. For example, the interior walls may be replacements of original walls. Under the recognition principle, an entity recognizes in the carrying amount of an investment property the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met. The carrying amount of those parts that are replaced is derecognized in accordance with the derecognition provisions of this Standard.

Measurement at Recognition

26. **Investment property shall be measured initially at its cost (transaction costs shall be included in this initial measurement).**

27. **Where an investment property is acquired through a non-exchange transaction, its cost shall be measured at its fair value as at the date of acquisition.**

28. The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure. Directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes, and other transaction costs

29. [Not used to maintain consistency of paragraph numbers with IPSASs]

30. The cost of investment property is not increased by:

    (a) Start-up costs (unless they are necessary to bring the property to the condition necessary for it to be capable of operating in the manner intended by management);

    (b) Operating losses incurred before the investment property achieves the planned level of occupancy; or

    (c) Abnormal amounts of wasted material, labor or other resources incurred in constructing or developing the property.

31. If payment for investment property is deferred, its cost is the cash price equivalent. The difference between this amount and the total payments is recognized as interest expense over the period of credit.

32. An investment property may be acquired through a non-exchange transaction. For example, a national government may transfer at no charge a surplus office building to a local government entity, which then lets it out at market rent. An investment property may also be acquired through a non-exchange transaction by the exercise of powers of sequestration. In these circumstances, the cost of the property is its fair value as at the date it is acquired.

33. Where an entity initially recognizes its investment property at fair value in accordance with paragraph 27, the fair value is the cost of the property. The entity shall decide, subsequent to initial recognition, to adopt either the fair value model (paragraphs 42–64) or the cost model (paragraph 65).

34. **The initial cost of a property interest held under a lease and classified as an investment property shall be as prescribed for a finance lease by paragraph 28 of SLPSAS 12, i.e., the asset shall be recognized at the lower of the fair value of the property and the present value of the minimum lease payments. An equivalent amount shall be recognized as a liability in accordance with that same paragraph.**

35. Any premium paid for a lease is treated as part of the minimum lease payments for this purpose, and is therefore included in the cost of the asset, but is excluded from the liability. If a property interest held under a lease is classified as investment property, the item accounted for at fair value is that interest and not the underlying property. Guidance on determining the fair value of a property interest is set out for the fair value model in paragraphs 42–61. That guidance is also relevant to the determination of fair value when that value is used as cost for initial recognition purposes.

36. One or more investment properties may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The following discussion refers to an exchange of one non-monetary asset for another, but it also applies to all exchanges described in the preceding sentence. The cost of such an investment property is measured at fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable. The acquired asset is measured in this way even if an entity cannot immediately derecognize the asset given up. If the acquired asset is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

37. An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows or service potential is expected to change as a result of the transaction. An exchange transaction has commercial substance if:

    (a) The configuration (risk, timing, and amount) of the cash flows or service potential of the asset received differs from the configuration of the cash flows or service potential of the asset transferred; or

    (b) The entity-specific value of the portion of the entity's operations affected by the transaction changes as a result of the exchange; and

    (c) The difference in (a) or (b) is significant relative to the fair value of the assets exchanged.

    For the purpose of determining whether an exchange transaction has commercial substance, the entity-specific value of the portion of the entity's operations affected by the transaction shall reflect post-tax cash flows, if tax applies. The result of these analyses may be clear without an entity having to perform detailed calculations.

38. The fair value of an asset for which comparable market transactions do not exist is reliably measurable if (a) the variability in the range of reasonable fair value estimates is not significant for that asset or (b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value. If the entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

Measurement after Recognition

Accounting Policy

39. **With the exception noted in paragraph 43, an entity shall choose as its accounting policy either the fair value model in paragraphs 42–64 or the cost model in paragraph 65, and shall apply that policy to all of its investment property.**

40. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors states that a voluntary change in accounting policy shall be made only if the change results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows. It is highly unlikely that a change from the fair value model to the cost model will result in a more relevant presentation.

41. This Standard requires all entities to determine the fair value of investment property, for the purpose of either measurement (if the entity uses the fair value model) or disclosure (if it uses the cost model). An entity is encouraged, but not required, to determine the fair value of investment property on the basis of a valuation by an independent valuer who holds a recognized and relevant professional qualification and has recent experience in the location and category of the investment property being valued.

Fair Value Model

42. **After initial recognition, an entity that chooses the fair value model shall measure all of its investment property at fair value, except in the cases described in paragraph 62.**

43. When a property interest held by a lessee under an operating lease is classified as an investment property under paragraph 8, paragraph 39 is not elective; the fair value model shall be applied.

44. **A gain or loss arising from a change in the fair value of investment property shall be recognized in surplus or deficit for the period in which it arises.**

45. The fair value of investment property is the price at which the property could be exchanged between knowledgeable, willing parties in an arm's length transaction (see paragraph 7). Fair value specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale.

46. An entity determines fair value without any deduction for transaction costs it may incur on sale or other disposal.

47. **The fair value of investment property shall reflect market conditions at the reporting date**.

48. Fair value is time-specific as of a given date. Because market conditions may change, the amount reported as fair value may be incorrect or inappropriate if estimated as of another time. The definition of fair value also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might be made in an arm's length transaction between knowledgeable, willing parties if exchange and completion are not simultaneous.

49. The fair value of investment property reflects, among other things, rental revenue from current leases and reasonable and supportable assumptions that represent what knowledgeable, willing parties would assume about rental revenue from future leases in the light of current conditions. It also reflects, on a similar basis, any cash outflows (including rental payments and other outflows) that could be expected in respect of the property. Some of those outflows are reflected in the liability whereas others relate to outflows that are not recognized in the financial statements until a later date (e.g. periodic payments such as contingent rents).

50. Paragraph 34 specifies the basis for initial recognition of the cost of an interest in a leased property. Paragraph 42 requires the interest in the leased property to be remeasured, if necessary, to fair value. In a lease negotiated at market rates, the fair value of an interest in a leased property at acquisition, net of all expected lease payments (including those relating to recognized liabilities), should be zero. This fair value does not change regardless of whether, for accounting purposes, a leased asset and liability are recognized at fair value or at the present value of minimum lease payments, in accordance with paragraph 28 of SLPSAS 12. Thus, remeasuring a leased asset from cost in accordance with paragraph 34 to fair value in accordance with paragraph 42 should not give rise to any initial gain or loss, unless fair value is measured at different times. This could occur when an election to apply the fair value model is made after initial recognition.

51. The definition of fair value refers to "knowledgeable, willing parties". In this context, "knowledgeable" means that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the investment property, its actual and potential uses, and market conditions at the reporting date. A willing buyer is motivated, but not compelled, to buy. This buyer is neither over-eager nor determined to buy at any price. The assumed buyer would not pay a higher price than a market comprising knowledgeable, willing buyers and sellers would require.

52. A willing seller is neither an over-eager nor a forced seller, prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in current market conditions. The willing seller is motivated to sell the investment property at market terms for the best price obtainable. The factual circumstances of the actual investment property owner are not a part of this consideration because the willing seller is a hypothetical owner (e.g., a willing seller would not take into account the particular tax circumstances of the actual investment property owner).

53. The definition of fair value refers to an arm's length transaction. An arm's length transaction is one between parties that do not have a particular or special relationship that makes prices of transactions uncharacteristic of market conditions. The transaction is presumed to be between unrelated parties, each acting independently.

54. The best evidence of fair value is given by current prices in an active market for similar property in the same location and condition and subject to similar lease and other contracts. An entity takes care to identify any differences in the nature, location, or condition of the property, or in the contractual terms of the leases and other contracts relating to the property.

55. In the absence of current prices in an active market of the kind described in paragraph 54, an entity considers information from a variety of sources, including:

    (a) Current prices in an active market for properties of different nature, condition, or location (or subject to different lease or other contracts), adjusted to reflect those differences;

    (b) Recent prices of similar properties on less active markets, with adjustments to reflect any changes in economic conditions since the date of the transactions that occurred at those prices; and

    (c) Discounted cash flow projections based on reliable estimates of future cash flows, supported by the terms of any existing lease and other contracts and (when possible) by external evidence, such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

56. In some cases, the various sources listed in the previous paragraph may suggest different conclusions about the fair value of an investment property. An entity considers the reasons for those differences, in order to arrive at the most reliable estimate of fair value within a range of reasonable fair value estimates.

57. In exceptional cases, there is clear evidence when an entity first acquires an investment property (or when an existing property first becomes an investment property after a change in use) that the variability in the range of reasonable fair value estimates will be so great, and the probabilities of the various outcomes so difficult to assess, that the usefulness of a single estimate of fair value is negated. This may indicate that the fair value of the property will not be reliably determinable on a continuing basis (see paragraph 62).

58. Fair value differs from value in use. Fair value reflects the knowledge and estimates of knowledgeable, willing buyers and sellers. In contrast, value in use reflects the entity's estimates, including the effects of factors that may be specific to the entity and not applicable to entities in general. For example, fair value does not reflect any of the following factors, to the extent that they would not be generally available to knowledgeable, willing buyers and sellers:

    (a) Additional value derived from the creation of a portfolio of properties in different locations;

    (b) Synergies between investment property and other assets;

    (c) Legal rights or legal restrictions that are specific only to the current owner; and

    (d) Tax benefits or tax burdens that are specific to the current owner.

59. In determining the carrying amount of investment property under the fair value model, an entity does not double-count assets or liabilities that are recognized as separate assets or liabilities. For example:

    (a) Equipment such as elevators or air-conditioning is often an integral part of a building and is generally included in the fair value of the investment property, rather than recognized separately as property, plant, and equipment.

    (b) If an office is leased on a furnished basis, the fair value of the office generally includes the fair value of the furniture, because the rental revenue relates to the furnished office. When furniture is included in the fair value of investment property, an entity does not recognize that furniture as a separate asset.

    (c) The fair value of investment property excludes prepaid or accrued operating lease revenue, because the entity recognizes it as a separate liability or asset.

(d) The fair value of investment property held under a lease reflects expected cash flows (including contingent rent that is expected to become payable). Accordingly, if a valuation obtained for a property is net of all payments expected to be made, it will be necessary to add back any recognized lease liability, to arrive at the carrying amount of the investment property using the fair value model.

60. The fair value of investment property does not reflect future capital expenditure that will improve or enhance the property and does not reflect the related future benefits from this future expenditure.

61. In some cases, an entity expects that the present value of its payments relating to an investment property (other than payments relating to recognized liabilities) will exceed the present value of the related cash receipts. An entity applies SLPSAS 8, Provisions, Contingent Liabilities and Contingent Assets to determine whether to recognize a liability and, if so, how to measure it.

Inability to Determine Fair Value Reliably

62. There is a rebuttable presumption that an entity can reliably determine the fair value of an investment property on a continuing basis. However, in exceptional cases, there is clear evidence when an entity first acquires an investment property (or when an existing property first becomes investment property after a change in use) that the fair value of the investment property is not reliably determinable on a continuing basis. This arises when, and only when, comparable market transactions are infrequent and alternative reliable estimates of fair value (for example, based on discounted cash flow projections) are not available. If an entity determines that the fair value of an investment property under construction is not reliably determinable but expects the fair value of the property to be reliably determinable when construction is complete, it shall measure that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed (whichever is earlier). If an entity determines that the fair value of an investment property (other than an investment property under construction) is not reliably determinable on a continuing basis, the entity shall measure that investment property using the cost model in SLPSAS 7. The residual value of the investment property shall be assumed to be zero. The entity shall apply SLPSAS 7 until disposal of the investment property.

62A. Once an entity becomes able to measure reliably the fair value of an investment property under construction that has previously been measured at cost, it shall measure that property at its fair value. Once construction of that property is complete, it is presumed that fair value can be measured reliably. If this is not the case, in accordance with paragraph 62, the property shall be accounted for using the cost model in accordance with SLPSAS 7.

62B. The presumption that the fair value of investment property under construction can be measured reliably can be rebutted only on initial recognition. An entity that has measured an item of investment property under construction at fair value may not conclude that the fair value of the completed investment property cannot be determined reliably.

63. In the exceptional cases when an entity is compelled, for the reason given in paragraph 62, to measure an investment property using the cost model in accordance with SLPSAS 7, it measures at fair value all its other investment property, including investment property under construction. In these cases, although an entity may use the cost model for one investment property, the entity shall continue to account for each of the remaining properties using the fair value model.

64. **If an entity has previously measured an investment property at fair value, it shall continue to measure the property at fair value until disposal (or until the property becomes owner-occupied property or the entity begins to develop the property for subsequent sale in the ordinary course of operations) even if comparable market transactions become less frequent or market prices become less readily available.**

Cost Model

65. **After initial recognition, an entity that chooses the cost model shall measure all of its investment property in accordance with SLPSAS 7's requirements for that model, i.e., at cost less any accumulated depreciation and any accumulated impairment losses.**

Transfers

66. **Transfers to or from investment property shall be made when, and only when, there is a change in use, evidenced by:**

   (a) **Commencement of owner-occupation, for a transfer from investment property to owner-occupied property;**

   (b) **Commencement of development with a view to sale, for a transfer from investment property to inventories;**

   (c) **End of owner-occupation, for a transfer from owner-occupied property to investment property; or**

   (d) **Commencement of an operating lease (on a commercial basis) to another party, for a transfer from inventories to investment property.**

67. A government's use of property may change over time. For example, a government may decide to occupy a building currently used as an investment property, or to convert a building currently used as naval quarters or for administrative purposes into a hotel and to let that building to private sector

operators. In the former case, the building would be accounted for as an investment property until commencement of occupation. In the latter case, the building would be accounted for as property, plant, and equipment until its occupation ceased and it is reclassified as an investment property.

68. Paragraph 66(b) requires an entity to transfer a property from investment property to inventories when, and only when, there is a change in use, evidenced by commencement of development with a view to sale. When an entity decides to dispose of an investment property without development, it continues to treat the property as an investment property until it is derecognized (eliminated from the statement of financial position) and does not treat it as inventory. Similarly, if an entity begins to redevelop an existing investment property for continued future use as investment property, the property remains an investment property and is not reclassified as owner-occupied property during the redevelopment.

69. A government property department may regularly review its buildings to determine whether they are meeting its requirements, and as part of that process may identify, and hold, certain buildings for sale. In this situation, the building may be considered inventory. However, if the government decided to hold the building for its ability to generate rent revenue and its capital appreciation potential, it would be reclassified as an investment property on commencement of any subsequent operating lease.

70. Paragraphs 71–76 apply to recognition and measurement issues that arise when an entity uses the fair value model for investment property. When an entity uses the cost model, transfers between investment property, owner-occupied property, and inventories do not change the carrying amount of the property transferred, and they do not change the cost of that property for measurement or disclosure purposes.

71. **For a transfer from investment property carried at fair value to owner-occupied property or inventories, the property's cost for subsequent accounting in accordance with SLPSAS 7 or SLPSAS 9, shall be its fair value at the date of change in use.**

72. **If an owner-occupied property becomes an investment property that will be carried at fair value, an entity shall apply SLPSAS 7 up to the date of change in use. The entity shall treat any difference at that date between the carrying amount of the property in accordance with SLPSAS 7, and its fair value in the same way as a revaluation in accordance with SLPSAS 7.**

73. Up to the date when an owner-occupied property becomes an investment property carried at fair value, an entity depreciates the property and recognizes any impairment losses that have occurred. The entity treats any difference at that date between the carrying amount of the property

in accordance with SLPSAS 7, and its fair value in the same way as a revaluation in accordance with SLPSAS 7. In other words:

(a) Any resulting decrease in the carrying amount of the property is recognized in surplus or deficit. However, to the extent that an amount is included in revaluation surplus for that property, the decrease is charged against that revaluation surplus.

(b) Any resulting increase in the carrying amount is treated as follows:

   (i) To the extent that the increase reverses a previous impairment loss for that property, the increase is recognized in surplus or deficit. The amount recognized in surplus or deficit does not exceed the amount needed to restore the carrying amount to the carrying amount that would have been determined (net of depreciation) if no impairment loss had been recognized.

   (ii) Any remaining part of the increase is credited directly to net assets/equity in revaluation surplus. On subsequent disposal of the investment property, the revaluation surplus included in net assets/equity may be transferred to accumulated surpluses or deficits. The transfer from revaluation surplus to accumulated surpluses or deficits is not made through surplus or deficit.

74. **For a transfer from inventories to investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount shall be recognized in surplus or deficit.**

75. The treatment of transfers from inventories to investment property that will be carried at fair value is consistent with the treatment of sales of inventories.

76. **When an entity completes the construction or development of a self-constructed investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount shall be recognized in surplus or deficit.**

Disposals

77. **An investment property shall be derecognized (eliminated from the statement of financial position) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits or service potential are expected from its disposal.**

78. The disposal of an investment property may be achieved by sale or by entering into a finance lease. In determining the date of disposal for investment property, an entity applies the criteria in SLPSAS 10 for recognizing revenue from the sale of goods and considers the related guidance in the Implementation

Guidance to SLPSAS 10. SLPSAS 12 applies to a disposal effected by entering into a finance lease and to a sale and leaseback.

79. If, in accordance with the recognition principle in paragraph 20, an entity recognizes in the carrying amount of an asset the cost of a replacement for part of an investment property, it derecognizes the carrying amount of the replaced part. For investment property accounted for using the cost model, a replaced part may not be a part that was depreciated separately. If it is not practicable for an entity to determine the carrying amount of the replaced part, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or constructed. Under the fair value model, the fair value of the investment property may already reflect that the part to be replaced has lost its value. In other cases it may be difficult to discern how much fair value should be reduced for the part being replaced. An alternative to reducing fair value for the replaced part, when it is not practical to do so, is to include the cost of the replacement in the carrying amount of the asset and then to reassess the fair value, as would be required for additions not involving replacement.

80. **Gains or losses arising from the retirement or disposal of investment property shall be determined as the difference between the net disposal proceeds and the carrying amount of the asset, and shall be recognized in surplus or deficit (unless SLPSAS 12 requires otherwise on a sale and leaseback) in the period of the retirement or disposal.**

81. The consideration receivable on disposal of an investment property is recognized initially at fair value. In particular, if payment for an investment property is deferred, the consideration received is recognized initially at the cash price equivalent. The difference between the nominal amount of the consideration and the cash price equivalent is recognized as interest revenue in accordance with SLPSAS 10, using the effective interest method.

82. An entity applies SLPSAS 8 or other standards, as appropriate, to any liabilities that it retains after disposal of an investment property.

83. **Compensation from third parties for investment property that was impaired, lost, or given up shall be recognized in surplus or deficit when the compensation becomes receivable**.

84. Impairments or losses of investment property, related claims for or payments of compensation from third parties, and any subsequent purchase or construction of replacement assets are separate economic events and are accounted for separately as follows:

    (a) Impairments of investment property are recognized;

    (b) Retirements or disposals of investment property are recognized in accordance with paragraphs 77–82 of this Standard;

(c) Compensation from third parties for investment property that was impaired, lost, or given up is recognized in surplus or deficit when it becomes receivable; and

(d) The cost of assets restored, purchased, or constructed as replacements is determined in accordance with paragraphs 26–38 of this Standard.

Disclosure

Fair Value Model and Cost Model

85. The disclosures below apply in addition to those in SLPSAS 12. In accordance with SLPSAS 12, the owner of an investment property provides lessors' disclosures about leases into which it has entered. An entity that holds an investment property under a finance lease or operating lease provides lessees' disclosures for finance leases and lessors' disclosures for any operating leases into which it has entered.

86. **An entity shall disclose:**

(a) **Whether it applies the fair value or the cost model;**

(b) **If it applies the fair value model, whether, and in what circumstances, property interests held under operating leases are classified and accounted for as investment property;**

(c) **When classification is difficult (see paragraph 18), the criteria it uses to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of operations;**

(d) **The methods and significant assumptions applied in determining the fair value of investment property, including a statement whether the determination of fair value was supported by market evidence, or was more heavily based on other factors (which the entity shall disclose) because of the nature of the property and lack of comparable market data;**

(e) **The extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognized and relevant professional qualification and has recent experience in the location and category of the investment property being valued. If there has been no such valuation, that fact shall be disclosed;**

(f) **The amounts recognized in surplus or deficit for:**

(i) **Rental revenue from investment property;**

(ii) **Direct operating expenses (including repairs and maintenance) arising from investment property that generated rental revenue during the period; and**

(iii) **Direct operating expenses (including repairs and maintenance) arising from investment property that did not generate rental revenue during the period.**

(g) **The existence and amounts of restrictions on the realizability of investment property or the remittance of revenue and proceeds of disposal; and**

(h) **Contractual obligations to purchase, construct, or develop investment property or for repairs, maintenance, or enhancements**.

Fair Value Model

87. **In addition to the disclosures required by paragraph 86, an entity that applies the fair value model in paragraphs 42–64 shall disclose a reconciliation between the carrying amounts of investment property at the beginning and end of the period, showing the following:**

(a) **Additions, disclosing separately those additions resulting from acquisitions and those resulting from subsequent expenditure recognized in the carrying amount of an asset;**

(b) **Additions resulting from acquisitions through entity combinations;**

(c) **Disposals;**

(d) **Net gains or losses from fair value adjustments;**

(e) **The net exchange differences arising on the translation of the financial statements into a different presentation currency, and on translation of a foreign operation into the presentation currency of the reporting entity;**

(f) **Transfers to and from inventories and owner-occupied property; and**

(g) **Other changes.**

88. **When a valuation obtained for investment property is adjusted significantly for the purpose of the financial statements, for example to avoid double-counting of assets or liabilities that are recognized as separate assets and liabilities as described in paragraph 59, the entity shall disclose a reconciliation between the valuation obtained and the adjusted valuation included in the financial statements, showing separately the aggregate amount of any recognized lease obligations that have been added back, and any other significant adjustments.**

89. **In the exceptional cases referred to in paragraph 62, when an entity measures investment property using the cost model in SLPSAS 7, the reconciliation required by paragraph 87 shall disclose amounts relating to that investment property separately from amounts relating to other investment property. In addition, an entity shall disclose:**

(a) **A description of the investment property;**

(b) **An explanation of why fair value cannot be determined reliably;**

(c) **If possible, the range of estimates within which fair value is highly likely to lie; and**

(d) **On disposal of investment property not carried at fair value:**

(i) **The fact that the entity has disposed of investment property not carried at fair value;**

(ii) **The carrying amount of that investment property at the time of sale; and**

(iii) **The amount of gain or loss recognized.**

Cost Model

90. **In addition to the disclosures required by paragraph 86, an entity that applies the cost model in paragraph 65 shall disclose:**

(a) **The depreciation methods used;**

(b) **The useful lives or the depreciation rates used;**

(c) **The gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period;**

(d) **The reconciliation of the carrying amount of investment property at the beginning and end of the period, showing the following:**

(i) **Additions, disclosing separately those additions resulting from acquisitions and those resulting from subsequent expenditure recognized as an asset;**

(ii) **Additions resulting from acquisitions through entity combinations;**

(iii) **Disposals;**

(iv) **Depreciation;**

(v) **The amount of impairment losses recognized, and the amount of impairment losses reversed, during the period;**

(vi) **The net exchange differences arising on the translation of the financial statements into a different presentation currency, and on translation of a foreign operation into the presentation currency of the reporting entity;**

(vii) **Transfers to and from inventories and owner-occupied property; and**

(viii) **Other changes; and**

(e) **The fair value of investment property. In the exceptional cases described in paragraph 62, when an entity cannot determine the fair value of the investment property reliably, the entity shall disclose:**

(i) **A description of the investment property;**

(ii) **An explanation of why fair value cannot be determined reliably; and**

(iii) **If possible, the range of estimates within which fair value is highly likely to lie.**

Transitional Provisions

Initial Adoption of Accrual Accounting

91. **An entity that adopts accrual accounting for the first time in accordance with SLPSASs shall initially recognize investment property at cost or fair value. For investment properties that were acquired at no cost, or for a nominal cost, cost is the investment property's fair value as at the date of acquisition.**

92. **The entity shall recognize the effect of the initial recognition of investment property as an adjustment to the opening balance of accumulated surpluses or deficits for the period in which accrual accounting is first adopted in accordance with SLPSASs.**

93. Prior to first adoption of accrual accounting in accordance with SLPSASs, an entity (a) may recognize investment property on a basis other than cost or fair value as defined in this Standard, or (b) may control investment property that it has not recognized. This Standard requires entities to initially recognize investment property at cost or fair value as at the date of first adoption of accrual accounting in accordance with SLPSASs. Where assets are initially recognized at cost and were acquired at no cost, or for a nominal cost, cost will be determined by reference to the investment property's fair value as at the date of acquisition. Where the cost of acquisition of an investment property is not known, its cost may be estimated by reference to its fair value as at the date of acquisition.

Fair Value Model

94. **Under the fair value model, an entity shall recognize the effect of applying this Standard as an adjustment to the opening balance of accumulated surpluses or deficits for the period in which this Standard is first applied. In addition:**

    (a) **If the entity has previously disclosed publicly (in financial statements or otherwise) the fair value of its investment property in earlier periods (determined on a basis that satisfies the definition of fair value in paragraph 7 and the guidance in paragraphs 45–61), the entity is encouraged, but not required:**

        (i) **To adjust the opening balance of accumulated surpluses or deficits for the earliest period presented for which such fair value was disclosed publicly; and**

        (ii) **To restate comparative information for those periods; and**

    (b) **If the entity has not previously disclosed publicly the information described in (a), it shall not restate comparative information and shall disclose that fact.**

95. On the first application of this Standard, an entity may choose to apply the fair value model in respect of investment property already recognized in its financial statements. When this occurs, this Standard requires any adjustment to the carrying amount of the investment property to be taken to the opening balance of accumulated surpluses or deficits for the period in which the Standard is first applied. This Standard requires a treatment different from that required by SLPSAS 3. SLPSAS 3 requires comparative information to be restated unless such restatement is impracticable. This Standard only encourages such comparative information to be restated in certain circumstances.

96. When an entity first applies this Standard, the adjustment to the opening balance of accumulated surpluses or deficits includes the reclassification of any amount held in revaluation surplus for investment property.

97. [Not used to maintain consistency of paragraph numbers with IPSASs]

Cost Model

98. Prior to first application of this Standard, an entity may recognize its investment property on a basis other than cost, for example fair value or some other measurement basis. SLPSAS 3 applies to any change in accounting policies that is made when an entity first applies this Standard and chooses to use the cost model. The effect of the change in accounting policies includes the reclassification of any amount held in revaluation surplus for investment property.

99. SLPSAS 3 requires an entity to retrospectively apply accounting policies unless it is impracticable to do so. Therefore, when an entity (a) initially recognizes investment property at cost, and (b) chooses to use the cost model in accordance with this Standard, it shall also recognize any accumulated depreciation and any accumulated impairment losses that relate to that property, as if it had always applied those accounting policies.

100. [Not used to maintain consistency of paragraph numbers with IPSASs]

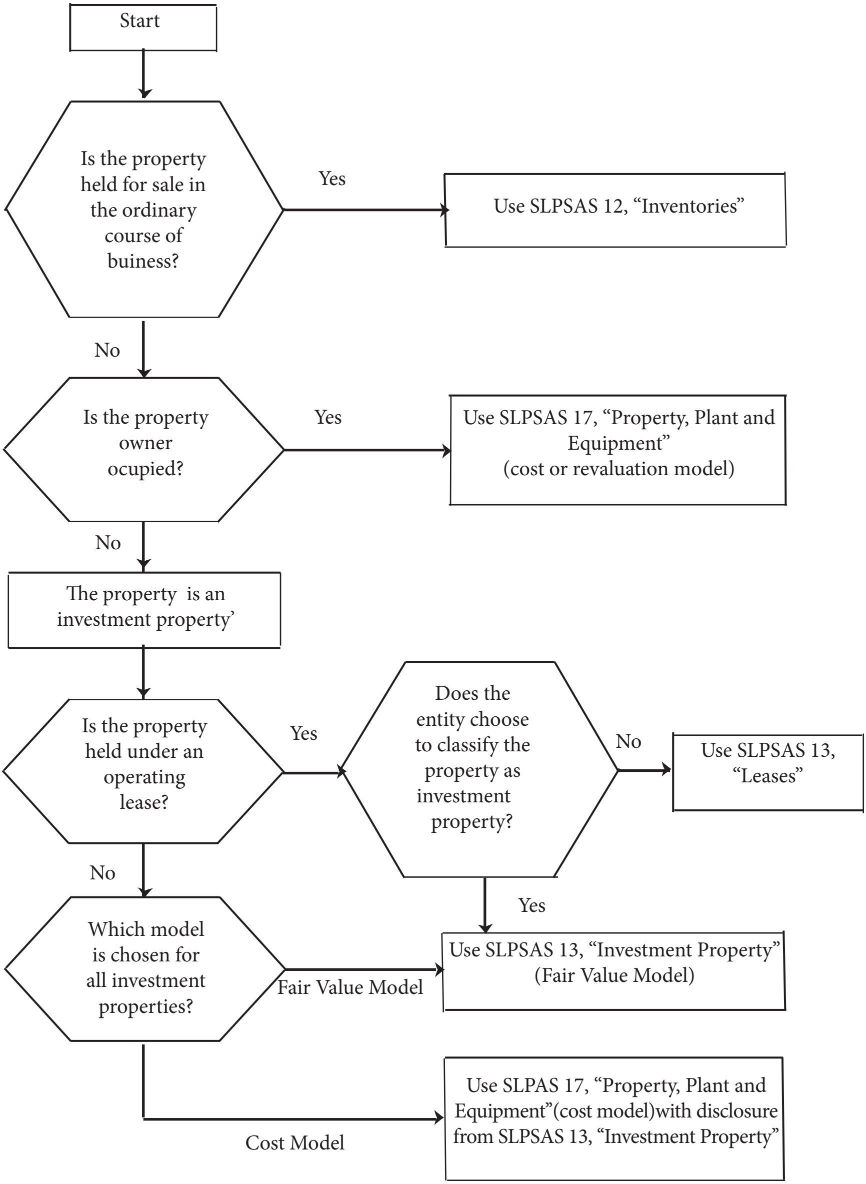
Effective Date

101. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1 2018, Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1 2018, it shall disclose that fact.**

102. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Illustrative Decision Tree

This decision tree accompanies, but is not part of, SLPSAS 13



SLPSAS – 14- Related Party Disclosures

Acknowledgement

Related Party Disclosures (SLPSAS – 14) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 14 - RELATED PARTY DISCLOSURES

CONTENTS

Sri Lanka Public Sector Accounting Standard 14, Related Party Disclosures, is set out in the objective and paragraphs 1-43. All the paragraphs have equal authority. SLPSAS 14 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

The objective of this Standard is to require the disclosure of the existence of related party relationships where control exists, and the disclosure of information about transactions between the entity and its related parties in certain circumstances. This information is required for accountability purposes, and to facilitate a better understanding of the financial position and performance of the reporting entity. The principal issues in disclosing information about related parties are (a) identifying which parties control or significantly influence the reporting entity, and (b) determining what information should be disclosed about transactions with those parties.

Scope

1. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in disclosing information about related party relationships and certain transactions with related parties.**

2. **This Standard applies to all public sector entities other than Government Business Enterprises.**

3. The *Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

Definitions

4. **The following terms are used in this Standard with the meanings specified**:

   <u>Close members of the family of an individual</u> are close relatives of the individual or members of the individual's immediate family who can be expected to influence, or be influenced by, that individual in their dealings with the entity.

   <u>Key management personnel</u> are:

   (a) **All directors or members of the governing body of the entity; and**

   (b) **Other persons having the authority and responsibility for planning, directing, and controlling the activities of the reporting entity. Where they meet this requirement, key management personnel include:**

      (i) **Where there is a member of the governing body of a whole-of-government entity who has the authority and responsibility for planning, directing, and controlling the** activities of the reporting entity, that member;

      (ii) **Any key advisors of that member; and**

(iii) **Unless already included in (a), the senior management group of the reporting entity, including the chief executive or permanent head of the reporting entity.**

Oversight means the supervision of the activities of an entity, with the authority and responsibility to control, or exercise significant influence over, the financial and operating decisions of the entity.

Related party means parties are considered to be related if one party has the ability to (a) control the other party, or (b) exercise significant influence over the other party in making financial and operating decisions, or if the related party entity and another entity are subject to common control. Related parties include:

(a) **Entities that directly, or indirectly through one or more intermediaries, control, or are controlled by, the reporting entity;**

(b) **Associates;**

(c) **Individuals owning, directly or indirectly, an interest in the reporting entity that gives them significant influence over the entity, and close members of the family of any such individual;**

(d) **Key management personnel, and close members of the family of key management personnel; and**

(e) **Entities in which a substantial ownership interest is held, directly or indirectly, by any person described in (c) or (d), or over which such a person is able to exercise significant influence.**

Related party transaction is a transfer of resources or obligations between related parties, regardless of whether a price is charged. Related party transactions exclude transactions with any other entity that is a related party solely because of its economic dependence on the reporting entity or the government of which it forms part.

Remuneration of key management personnel is any consideration or benefit derived directly or indirectly by key management personnel from the reporting entity for services provided in their capacity as members of the governing body, or otherwise as employees of the reporting entity.

Significant influence (for the purpose of this Standard) is the power to participate in the financial and operating policy decisions of an entity, but not control those policies. Significant influence may be exercised in several ways, usually by representation on the board of directors or equivalent governing body but also by, for example, participation in (a) the policy making process, (b) material transactions between entities within an economic entity, (c) interchange of managerial personnel, or (d) dependence on technical information. Significant influence may be gained by an ownership interest, statute, or agreement.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of *Defined Terms* published separately.

Close Member of the Family of an Individual

5. Judgment will be necessary in determining whether an individual should be identified as a close member of the family of an individual for purposes of application of this Standard. In the absence of information to the contrary, such as that a spouse or other relative is estranged from the individual, the following immediate family members and close relatives are presumed to have, or be subject to, such influence as to satisfy the definition of close members of the family of an individual:

   (a) A spouse, domestic partner, dependent child, or relative living in a common household;

   (b) A grandparent, parent, nondependent child, grandchild, brother, or sister; and

   (c) The spouse or domestic partner of a child, a parent-in-law, a brother-in-law, or a sister-in-law.

Key Management Personnel

6. Key management personnel include all directors or members of the governing body of the reporting entity, where that body has the authority and responsibility for planning, directing, and controlling the activities of the entity. At the whole-of-government level, the governing body may consist of elected or appointed representatives (for example, a president or governor, ministers, councilors and aldermen or their nominees).

7. Where an entity is subject to the oversight of an elected or appointed representative of the governing body of the government to which the entity belongs, that person is included in key management personnel, if the oversight function includes the authority and responsibility for planning, directing, and controlling the activities of the entity. In many jurisdictions, key advisors of that person may not possess sufficient authority, legal or otherwise, to satisfy the definition of key management personnel. In other jurisdictions, key advisors of that person may be deemed to be key management personnel because they have a special working relationship with an individual who has control over an entity. They therefore have access to privileged information, and may also be able to exercise control or significant influence over an entity. Judgment is required in assessing whether an individual is a key advisor, and whether that advisor satisfies the definition of key management personnel, or is a related party.

8. The governing body, together with the chief executive and senior management group, has the authority and responsibility to plan and control the activities of the entity, to manage the resources of the entity and for

the overall achievement of entity objectives. Therefore, key management personnel will include the chief executive and senior management group of the reporting entity. In some jurisdictions, civil servants will not have sufficient authority and responsibility to qualify as key management personnel (as defined by this Standard) of the whole-of-government reporting entity. In these cases, key management personnel will consist only of those elected members of the governing body who have the greatest responsibility for the government; often these persons are referred to as Cabinet Ministers.

9. The senior management group of an economic entity may comprise individuals from both the controlling entity and other entities that collectively make up the economic entity.

Related Parties

10. In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

11. Where two entities have a member of key management personnel in common, it is necessary to consider the possibility, and to assess the likelihood, that this person would be able to affect the policies of both entities in their mutual dealings. However, the mere fact that there is a member of key management personnel in common does not necessarily create a related party relationship.

12. In the context of this Standard, the following are deemed not to be related parties:

    (a) (i) Providers of finance in the course of their business in that regard; and

    (ii) Trade unions;

    in the course of their normal dealings with an entity by virtue only of those dealings (although they may circumscribe the freedom of action of an entity or participate in its decision-making process); and

    (b) An entity with which the relationship is solely that of an agency.

13. Related party relationships may arise when an individual is either a member of the governing body or is involved in the financial and operating decisions of the reporting entity. Related party relationships may also arise through external operating relationships between the reporting entity and the related party. Such relationships will often involve a degree of economic dependency.

14. Economic dependency, where one entity is dependent on another in that it relies on the latter for a significant volume of its funding or sale of its goods and services, would on its own be unlikely to lead to control or significant influence and is therefore unlikely to give rise to a related party relationship. As such, a single customer, supplier, franchisor, distributor, or general agent with whom a public sector entity transacts a significant volume of business will not be a related party merely by virtue of the resulting economic dependency. However, economic dependency,

together with other factors, may give rise to significant influence, and therefore a related party relationship. Judgment is required in assessing the impact of economic dependence on a relationship. Where the reporting entity is economically dependent on another entity, the reporting entity is encouraged to disclose the existence of that dependency.

15. The definition of related party includes entities owned by key management personnel, close family members of such individuals or major shareholders (or equivalent where the entity does not have a formal equity structure) of the reporting entity. The definition of related party also includes circumstances in which one party has the ability to exercise significant influence over the other party. In the public sector, an individual or entity may be given oversight responsibility for a reporting entity, which gives them significant influence, but not control, over the financial and operating decisions of the reporting entity. For the purposes of this Standard, significant influence is defined to encompass entities subject to joint control.

Remuneration of Key Management Personnel

16. Remuneration of key management personnel includes remuneration derived by individuals from the reporting entity for services provided to the reporting entity in their capacity as members of the governing body or employees. Benefits derived directly or indirectly from the entity for services in any capacity, other than as an employee or a member of the governing body, do not satisfy the definition of remuneration of key management personnel in this Standard. However, paragraph 34 requires disclosures to be made about certain of these other benefits. Remuneration of key management personnel excludes any consideration provided solely as a reimbursement for expenditure incurred by those individuals for the benefit of the reporting entity, such as the reimbursement of accommodation costs associated with work-related travel.

Voting Power

17. The definition of related party will include any individuals owning, directly or indirectly, an interest in the voting power of the reporting entity that gives them significant influence over the entity. The holding of an interest in the voting power of an entity can arise when a public sector entity has a corporate structure, and a minister or government agency holds shares in the entity.

The Related Party Issue

18. Related party relationships exist throughout the public sector, because:

    (a) Administrative units are subject to the overall direction of the executive government and, ultimately, the Parliament or similar body of elected or appointed officials, and operate together to achieve the policies of the government;

    (b) Government departments and agencies frequently conduct activities necessary for the achievement of different components of their responsibilities and objectives through separate controlled entities, and through entities over which they have significant influence; and

(c) Ministers or other elected or appointed members of the government and senior management group can exert significant influence over the operations of a department or agency.

19. Disclosure of certain related party relationships and related party transactions and the relationship underlying those transactions is necessary for accountability purposes, and enables users to better understand the financial statements of the reporting entity because:

(a) Related party relationships can influence the way in which an entity operates with other entities in achieving its individual objectives, and the way in which it co-operates with other entities in achieving common or collective objectives;

(b) Related party relationships might expose an entity to risks, or provide opportunities that would not have existed in the absence of the relationship; and

(c) Related parties may enter into transactions that unrelated parties would not enter into, or may agree to transactions on different terms and conditions than those that would normally be available to unrelated parties. This occurs frequently in government departments and agencies, where goods and services are transferred between departments at less than full cost recovery as a part of normal operating procedures consistent with the achievement of the objectives of the reporting entity and the government. Governments and individual public sector entities are expected to use resources efficiently, effectively, and in the manner intended, and to deal with public monies with the highest levels of integrity. The existence of related party relationships means that one party can control or significantly influence the activities of another party. This provides the opportunity for transactions to occur on a basis that may advantage one party inappropriately at the expense of another.

20. Disclosure of certain types of related party transactions that occur, and the terms and conditions on which they were conducted, allows users to assess the impact of those transactions on the financial position and performance of an entity, and its ability to deliver agreed services. This disclosure also ensures that the entity is transparent about its dealings with related parties.

Remuneration of Key Management Personnel

21. Key management personnel hold positions of responsibility within an entity. They are responsible for the strategic direction and operational management of an entity, and are entrusted with significant authority. Their salaries are often established by statute, or an independent tribunal or other body independent of the reporting entity. However, their responsibilities

may enable them to influence the benefits of office that flow to them or their related parties. This Standard requires certain disclosures to be made about (a) the remuneration of key management personnel and close members of the family of key management personnel during the reporting period, (b) loans made to them, and (c) the consideration provided to them for services they provide to the entity other than as a member of the governing body or an employee. The disclosures required by this Standard will ensure that appropriate minimum levels of transparency are applied to the remuneration of key management personnel and close members of the family of key management personnel.

Materiality

22. SLPSAS 1 requires the separate disclosure of material items. The materiality of an item is determined with reference to the nature or size of that item. When assessing the materiality of related party transactions, the nature of the relationship between the reporting entity and the related party, and the nature of the transaction, may mean that a transaction is material regardless of its size.

Disclosure

23. In many countries, the laws and other authoritative financial reporting rules require financial statements of private sector entities and government business enterprises to disclose information about certain categories of related parties and related party transactions. In particular, attention is focused on the entity's transactions with its directors or members of its governing body and with its senior management group, especially their remuneration and borrowings. This is (a) because of the fiduciary responsibilities of directors, members of the governing body, and senior management group, and (b) because they have extensive powers over the deployment of entity resources. In some jurisdictions, similar requirements are included in the statutes and regulations applicable to public sector entities.

24. Some SLPSASs also require disclosure of transactions with related parties. For example, SLPSAS 1 requires disclosure of amounts payable to and receivable from controlling entities, fellow controlled entities, associates, and other related parties.

Disclosure of Control

25. **Related party relationships where control exists shall be disclosed, irrespective of whether there have been transactions between the related parties**.

26. In order for a reader of financial statements to form a view about the effects of related party relationships on a reporting entity, it is appropriate to disclose related party relationships where control exists, irrespective of whether there have been transactions between the related parties. This

would involve the disclosure of the names of any controlled entities, the name of the immediate controlling entity, and the name of the ultimate controlling entity, if any.

Disclosure of Related Party Transactions

27. **In respect of transactions between related parties, other than transactions that would occur within a normal supplier or client/recipient relationship on terms and conditions no more or less favorable than those which it is reasonable to expect the entity would have adopted if dealing with that individual or entity at arm's length in the same circumstances, the reporting entity shall disclose:**

    (a) **The nature of the related party relationships;**

    (b) **The types of transactions that have occurred; and**

    (c) **The elements of the transactions necessary to clarify the significance of these transactions to its operations and sufficient to enable the financial statements to provide relevant and reliable information for decision making and accountability purposes.**

28. The following are examples of situations where related party transactions may lead to disclosures by a reporting entity:

    (a) Rendering or receiving of services;

    (b) Purchases or transfers/sales of goods (finished or unfinished);

    (c) Purchases or transfers/sales of property and other assets;

    (d) Agency arrangements;

    (e) Leasing arrangements;

    (f) Transfer of research and development;

    (g) License agreements;

    (h) Finance (including loans, capital contributions, grants whether in cash or in kind, and other financial support, including cost-sharing arrangements); and

    (i) Guarantees and collaterals.

29. Public sector entities transact extensively with each other on a daily basis. These transactions may occur at cost, less than cost or free of charge. For example, a government department of administrative services may provide office accommodation free of charge to other departments, or a public sector entity may act as a purchasing agent for other public sector entities. In some models of government, there may be the capacity for recovery of more than the full cost of service delivery. Departments are related parties because they are subject to common control, and these transactions meet the definition of related party transactions. However,

disclosure of information about transactions between these entities is not required where the transactions (a) are consistent with normal operating relationships between the entities, and (b) are undertaken on terms and conditions that are normal for such transactions in these circumstances. The exclusion of these related party transactions from the disclosure requirements of paragraph 27 reflects that public sector entities operate together to achieve common objectives, and acknowledges that different mechanisms may be adopted for the delivery of services by public sector entities in different jurisdictions. This Standard requires disclosures of related party transactions only when those transactions occur other than in accordance with the operating parameters established in that jurisdiction.

30. The information about related party transactions that would need to be disclosed to meet the objectives of general purpose financial reporting would normally include:

    (a) A description of the nature of the relationship with related parties involved in these transactions, for example, whether the relationship was one of a controlling entity, a controlled entity, an entity under common control, or key management personnel;

    (b) A description of the related party transactions within each broad class of transaction and an indication of the volume of the classes, either as a specific monetary amount or as a proportion of that class of transactions and/or balances;

    (c) A summary of the broad terms and conditions of transactions with related parties, including disclosure of how these terms and conditions differ from those normally associated with similar transactions with unrelated parties; and

    (d) Amounts or appropriate proportions of outstanding items.

31. Paragraph 34 of this Standard requires additional disclosures to be made about certain transactions between an entity and key management personnel and/or the close members of the family of key management personnel.

32. **Items of a similar nature may be disclosed in aggregate, except when separate disclosure is necessary to provide relevant and reliable information for decision-making and accountability purposes.**

33. Disclosure of related party transactions between members of an economic entity is unnecessary in consolidated financial statements, because consolidated financial statements present information about the controlling entity and controlled entities as a single reporting entity. Related party transactions that occur between entities within an economic entity are eliminated on consolidation. Transactions with associated entities accounted for under the equity method are not eliminated, and therefore require separate disclosure as related party transactions.

Disclosure—Key Management Personnel

34. **An entity shall disclose**:

    (a) **The aggregate remuneration of key management personnel and the number of individuals, determined on a full-time equivalent basis, receiving remuneration within this category, showing separately major classes of key management personnel and including a description of each class;**

    (b) **The total amount of all other remuneration and compensation provided to key management personnel, and close members of the family of key management personnel, by the reporting entity during the reporting period, showing separately the aggregate amounts provided to:**

        (i) **Key management personnel; and**

        (ii) **Close members of the family of key management personnel; and**

    (c) **In respect of loans that are not widely available to persons who are not key management personnel and loans whose availability is not widely known by members of the public, for each individual member of key management personnel and each close member of the family of key management personnel:**

        (i) **The amount of loans advanced during the period and terms and conditions thereof;**

        (ii) **The amount of loans repaid during the period;**

        (iii) **The amount of the closing balance of all loans and receivables; and**

        (iv) **Where the individual is not a director or member of the governing body or senior management group of the entity, the relationship of the individual to such body or group.**

35. Paragraph 27 of this Standard requires the disclosure of related party transactions that have occurred other than on an arm's length basis consistent with the operating conditions established for the entity. This Standard also requires the disclosure of information about certain transactions with key management personnel identified in paragraph 34, whether or not they have occurred on an arm's length basis consistent with the operating conditions that apply in respect of the entity.

36. Persons who are key management personnel may be employed on a full- or part-time basis. The number of individuals disclosed as receiving remuneration in accordance with paragraph 34(a) needs to be estimated on a full-time equivalent basis. Entities will make separate disclosures

about the major classes of key management personnel that they have. For example, where an entity has a governing body that is separate from its senior management group, disclosures about remuneration of the two groups will be made separately. Where an individual is a member of both the governing body and the senior management group, that individual will be included in only one of those groups for the purposes of this Standard. The categories of key management personnel identified in the definition of key management personnel provide a guide to identifying classes of key management personnel.

37. Remuneration of key management personnel can include a variety of direct and indirect benefits. Where the cost of these benefits is determinable, that cost will be included in the aggregate remuneration disclosed. Where the cost of these benefits is not determinable, a best estimate of the cost to the reporting entity or entities will be made and included in the aggregate remuneration disclosed.

38. Requirements on the measurement of employee benefits are found in SLPSAS 19, Employee Benefits. When non-monetary remuneration that is able to be reliably measured has been included in the aggregate amount of remuneration of key management personnel disclosed for the period, disclosure would also be made in the notes to the financial statements of the basis of measurement of the non-monetary remuneration.

39. This Standard requires the disclosure of certain information about the terms and conditions of loans made to key management personnel and close members of the family of key management personnel, where these loans:

    (a) Are not widely available to persons outside the key management group; and

    (b) May be widely available outside the key management group, but whose availability is not widely known to members of the public.

    The disclosure of this information is required for accountability purposes. The exercise of judgment may be necessary in determining which loans should be disclosed to satisfy the requirements of this Standard. That judgment should be exercised after consideration of the relevant facts, and in a manner consistent with the achievement of the objectives of financial reporting.

40. Paragraph 34(a) of this Standard requires disclosure of the aggregate remuneration of key management personnel. Key management personnel include directors or members of the governing body and members of the senior management group of the entity. Directors or members of the governing body of the entity may also receive remuneration or compensation from the entity for services provided in a capacity other than (a) as director or member of the governing body of the entity, or (b) as an employee of the entity. Paragraph 34(b)(i) of this Standard requires the disclosure of the total amount of this other remuneration or compensation.

41. Close members of the family of key management personnel may influence, or be influenced by, key management personnel in their transactions with the reporting entity. Paragraph 34(b)(ii) of this Standard requires the disclosure of the total remuneration and compensation provided during the period to close members of the family of key management personnel.

Effective Date

42. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1 2018, Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1 2018, it shall disclose that fact.**

43. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Implementation Guidance

This guidance accompanies, but is not part of, SLPSAS 14.

Disclosure—Government X

The following disclosures are made in the financial statements of Government X.

Controlled Entities (Paragraph 25)

The Government controls the following reporting entities:

Government Departments and Agencies: Education, Welfare, Police, Post, Works and Services, Defense, Justice, Treasury/Finance, Department X, Agency XYZ (identify all departments and agencies).

Government Business Enterprises: Government Electricity Company, Government Telecommunications Agency (identify all GBEs).

Related Party Transactions (Paragraph 27)

A member of Cabinet was provided with a house, rent free, in the national Capital City. Houses similar to that provided to the Minister rent for approximately Z rupees per annum. The provision of accommodation is not part of the remuneration package of the Minister, and the Government does not generally provide free accommodation to ministers. However, in this case it was necessary to provide a residence for the Minister in the Capital City.

The partner of another member of Cabinet was provided with a motor vehicle, rent free. Cars similar to that provided normally rent for K rupees per annum. The government does not generally provide motor vehicles, rent free, to the domestic partners of ministers.

Key Management Personnel (Paragraph 34)

Remuneration (Paragraph 34(a))

The key management personnel (as defined by SLPSAS 14, Related Party Disclosures) are the members of Cabinet, who together constitute the governing body of Government X. The aggregate remuneration of members of the Cabinet and the number of individuals determined on a full-time equivalent basis receiving remuneration from Government X are:

Aggregate remuneration	X million.
Number of persons	Y persons.

Loans That are not Widely Available (and/or Widely Known) to Persons Outside the Key Management Group (paragraph 34(c))

Amounts of such loans advanced and repaid during the period, and the balances outstanding at the end of the period, are outlined below:

Individual	Advanced	Repaid	Balance
The Honorable ABC	J	K	L
Ms. VSL	M	N	P
The Honorable D	Q	R	Z
The Honorable E	S	T	U

Terms and Conditions

The Honorable ABC, Minister of Transport, received a loan at X% per annum, which is Y% below the market rate. The term of the loan is for Z years.

Ms. VSL, partner of the Minister of Health, received a government loan. The loan is for N years at X% per annum, the current government borrowing rate.

The salary packages of Cabinet Ministers the Honorable D and E allow them to take out a government loan for up to A years at Y% per annum to purchase a car.

Other Remuneration and Compensation Provided to Key Management Personnel and their Close Family Members (paragraph 34(b))

During the reporting period, total compensation of X amount (rupees) was provided to members of the Cabinet for consulting services provided to particular government agencies.

During the reporting period, the government provided total remuneration and compensation of Y amount (rupees) to close family members of key management personnel. This amount consists of the remuneration of government employees who are close members of the family of members of the Cabinet.

Disclosure - Government Agency XYZ

These disclosures are made in the financial statements of Government Agency XYZ, which is a separate reporting entity.

Controlled Entities (Paragraph 25)
The Agency is controlled by Department X. Department X is controlled by Government X.

The Agency controls the Administration Services Unit, which is a government business enterprise (GBE).

Related Party Transactions (Paragraph 27)

The Agency provided a house, rent free, to the Minister. Houses similar to that provided to the Minister rent for approximately Z rupees per annum. The house is not part of the remuneration package of the Minister and, as a matter of operating procedure, government agencies do not provide residential accommodation to ministers. However, Government X advised that the house should be provided on this occasion.

Key Management Personnel (Paragraph 34)

Remuneration (Paragraph 34(a))

The key management personnel (as defined by SLPSAS 14) of Agency XYZ are the Minister, the members of the governing body, and the members of the senior management group. The governing body consists of members appointed by Government X; the chief executive officer and the chief financial officer attend meetings of the governing body but are not members of the governing body. The Minister is not remunerated by Agency XYZ. The aggregate remuneration of members of the governing body and the number of members determined on a fulltime equivalent basis receiving remuneration within this category, are:

Aggregate remuneration	AX million.
Number of persons	AY persons.

The senior management group consists of the Agency's chief executive officer, the chief financial officer, and the AZ heads of division. The aggregate remuneration of members of the senior management group and the number of managers determined on a full-time equivalent basis receiving remuneration within this category are:

Aggregate remuneration	AP million.
Number of persons	AQ persons.

Two division heads are on secondment from Department X, and are remunerated by Department X.

Loans That are not Widely Available (and/or Widely Known) to Persons Outside the Key Management Group (paragraph 34(c))

Amounts advanced and repaid during the period and balance outstanding at the end of the period:

Individual	Advanced	Repaid	Balance
The Minister	J	K	L
Mr. G	M	N	P
Ms. H	Q	R	Z

Terms and Conditions

The Minister received a loan of J rupees, at X% per annum, which is Y% below the market rate. The term of the loan is for Z years.
The salary package of senior staff members, Mr. G and Ms. H, allows them to take out a government loan for up to N years at Y% per annum to purchase a car.

Remuneration and Compensation Provided to Close Family Members of Key Management Personnel (paragraph 34(b))

During the reporting period, total remuneration and compensation of F amount (rupees) was provided by the Agency to employees who are close family members of key management personnel.

SLPSAS – 15 - Presentation of Budget Information in Financial Statements

Acknowledgement

Presentation of Budget Information in Financial Statements (SLPSAS – 15) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 15 - PRESENTATION BUDGET INFORMATION IN FINANCIAL STATEMENTS

CONTENTS

Sri Lanka Public Sector Accounting Standard 15, Presentation of Budget Information in Financial Statements, is set out in paragraphs 1-55. All the paragraphs have equal authority. SLPSAS 15 should be read in the context of its objective and the Preface to the Sri Lanka Public Sector Accounting Standards. IPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. This Standard requires a comparison of budget amounts and the actual amounts arising from execution of the budget to be included in the financial statements of entities that are required to, or elect to, make publicly available their approved budget(s), and for which they are, therefore, held publicly accountable. This Standard also requires disclosure of an explanation of the reasons for material differences between the budget and actual amounts. Compliance with the requirements of this Standard will ensure that public sector entities discharge their accountability obligations and enhance the transparency of their financial statements by demonstrating (a) compliance with the approved budget(s) for which they are held publicly accountable and (b) where the budget(s) and the financial statements are prepared on the same basis, their financial performance in achieving the budgeted results.

Scope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard.**

3. **This Standard applies to public sector entities, other than Government Business Enterprises, which are required or elect to make their approved budget(s) publicly available.**

4. The *Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

5. This Standard does not require approved budgets to be made publicly available, nor does it require that the financial statements disclose information about, or make comparisons with, approved budgets that are not made publicly available.

6. In some cases, approved budgets will be compiled to encompass all the activities controlled by a public sector entity. In other cases, separate approved budgets may be required to be made publicly available for certain activities, groups of activities, or entities included in the financial statements of a government or other public sector entity. This may occur (a) where, for example, a government's financial statements encompass government agencies or programs that have operational autonomy and prepare their own budgets, or (b) where a budget is prepared only for the general government sector of the whole-of-government. This Standard applies to all entities that present financial statements when approved budgets for the entity, or components thereof, are made publicly available.

Definitions

7. **The following terms are used in this Standard with the meanings specified:**

Accounting basis means the accrual or cash basis of accounting. Accrual basis is defined in SLPSAS 1.

Annual budget means an approved budget for one year. It does not include published forward estimates or projections for periods beyond the budget period.

Appropriation is an authorization granted by a legislative body to allocate funds for purposes specified by the legislature or similar authority.

Approved budget means the expenditure authority derived from laws, appropriation bills, government ordinances, and other decisions related to the anticipated revenue or receipts for the budgetary period.

Budgetary basis means the accrual, cash, or other basis of accounting adopted in the budget that has been approved by the legislative body.

Comparable basis means the actual amounts presented on the same accounting basis, same classification basis, for the same entities, and for the same period as the approved budget.

Final budget is the original budget, adjusted for all reserves, carry-over amounts, transfers, allocations, supplemental appropriations, and other authorized legislative or similar authority changes applicable to the budget period.

Multi-year budget is an approved budget for more than one year. It does not include published forward estimates or projections for periods beyond the budget period.

Original budget is the initial approved budget for the budget period.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of *Defined Terms published separately.*

Approved Budgets

8. An approved budget as defined by this Standard reflects the anticipated revenues or receipts expected to arise in the annual or multi-year budget period, based on current plans and the anticipated economic conditions during that budget period, and expenses or expenditures approved by a legislative body, being the legislature or other relevant authority. An approved budget is not a forward estimate, or a projection based on assumptions about future events and possible management actions that are not necessarily expected to take place. Similarly, an approved budget differs from prospective financial information, which may be in the form

of a forecast, a projection, or a combination of both; for example, a one-year forecast plus a five-year projection.

9. In some jurisdictions, budgets may be signed into law as part of the approval process. In other jurisdictions, approval may be provided without the budget becoming law. Whatever the approval process, the critical feature of approved budgets is that the authority to withdraw funds from the government treasury or similar body for agreed and identified purposes is provided by a higher legislative body or other appropriate authority. The approved budget establishes the expenditure authority for the specified items. The expenditure authority is generally considered the legal limit within which an entity must operate. In some jurisdictions, the approved budget for which the entity will be held accountable may be the original budget, and in others it may be the final budget.

10. If a budget is not approved prior to the beginning of the budget period, the original budget is the budget that was first approved for application in the budget year.

Original and Final Budget

11. The original budget may include residual appropriated amounts automatically carried over from prior years by law. For example, governmental budgetary processes in some jurisdictions include a legal provision that requires the automatic rolling forward of appropriations to cover prior year commitments. Commitments encompass possible future liabilities based on a current contractual agreement. In some jurisdictions, they may be referred to as obligations or encumbrances, and include outstanding purchase orders and contracts where goods or services have not yet been received.

12. Supplemental appropriations may be necessary where the original budget did not adequately envisage expenditure requirements arising from, for example, war or natural disasters. In addition, there may be a shortfall in budgeted revenues during the period, and internal transfers between budget heads or line items may be necessary to accommodate changes in funding priorities during the fiscal period. Consequently, the funds allotted to an entity or activity may need to be cut back from the amount originally appropriated for the period in order to maintain fiscal discipline. The final budget includes all such authorized changes or amendments.

Actual Amounts

13. This Standard uses the term actual or actual amount to describe the amounts that result from execution of the budget. In some jurisdictions, budget outturn, budget execution, or similar terms may be used with the same meaning as actual or actual amount.

Presentation of a Comparison of Budget and Actual Amounts

14. **Subject to the requirements of paragraph 21, an entity shall present a comparison of the budget amounts for which it is held publicly accountable and actual amounts, either as a separate additional financial statement or as additional budget columns in the financial statements currently presented in accordance with SLPSASs. The comparison of budget and actual amounts shall present separately for each level of legislative oversight:**

    (a) **The original and final budget amounts**;

    (b) **The actual amounts on a comparable basis; and**

    (c) **By way of note disclosure, an explanation of material differences between the budget for which the entity is held publicly accountable and actual amounts, unless such explanation is included in other public documents issued in conjunction with the financial statements, and a cross reference to those documents is made in the notes.**

15. Presentation in the financial statements of the original and final budget amounts and actual amounts on a comparable basis with the budget that is made publicly available will complete the accountability cycle by enabling users of the financial statements to identify whether resources were obtained and used in accordance with the approved budget. Differences between the actual amounts and the budget amounts, whether original or final budget (often referred to as the variance in accounting), may also be presented in the financial statements for completeness.

16. An explanation of the material differences between actual amounts and the budget amounts will assist users in understanding the reasons for material departures from the approved budget for which the entity is held publicly accountable.

17. An entity may be required, or may elect, to make publicly available its original budget, its final budget, or both its original and final budget. In circumstances where both the original and final budget are required to be made publicly available, the legislation, regulation, or other authority will often provide guidance on whether explanation of material differences between the actual and the original budget amounts, or actual and the final budget amounts, is required in accordance with paragraph 14(c). In the absence of any such guidance, material differences may be determined by reference to, for example, (a) differences between actual and original budget to focus on performance against original budget, or (b) differences between actual and final budget to focus on compliance with the final budget.

18. In many cases, the final budget and the actual amount will be the same. This is because budget execution is monitored over the reporting period, and the original budget progressively revised to reflect changing conditions, changing circumstances, and experiences during the reporting period. Paragraph 29 of this Standard requires the disclosure of an explanation of the reasons for changes between the original and final budget. Those disclosures, together with the disclosures required by paragraph 14 above, will ensure that entities that make publicly available their approved budget(s) are held publicly accountable for their performance against, and compliance with, the relevant approved budget.

19. Management discussion and analysis, operations review, or other public reports that provide commentary on the performance and achievements of the entity during the reporting period, including explanations of any material differences from budget amounts, are often issued in conjunction with the financial statements. In accordance with paragraph 14(c) of this Standard, explanation of material differences between actual and budget amounts will be included in notes to the financial statements, unless (a) included in other public reports or documents issued in conjunction with the financial statements, and (b) the notes to the financial statements identify the reports or documents in which the explanation can be found.

20. Where approved budgets are only made publicly available for some of the entities or activities included in the financial statements, the requirements of paragraph 14 will apply to only the entities or activities reflected in the approved budget. This means that where, for example, a budget is prepared only for the general government sector of a whole-of-government reporting entity, the disclosures required by paragraph 14 will be made only in respect of the general government sector of the government.

Presentation and Disclosure

21. **An entity shall present a comparison of budget and actual amounts as additional budget columns in the primary financial statements only where the financial statements and the budget are prepared on a comparable basis.**

22. Comparisons of budget and actual amounts may be presented in a separate financial statement, (Statement of Comparison of Budget and Actual Amounts or a similarly titled statement) included in the complete set of financial statements as specified in SLPSAS 1. Alternatively, where the financial statements and the budget are prepared on a comparable basis – that is, on the same basis of accounting for the same entity and reporting period, and adopt the same classification structure – additional columns may be added to the existing primary financial statements presented in accordance with SLPSASs. These additional columns will identify original and final budget amounts and, if the entity so chooses, differences between the budget and actual amounts.

23. When the budget and financial statements are not prepared on a comparable basis, a separate Statement of Comparison of Budget and Actual Amounts is presented. In these cases, to ensure that readers do not misinterpret financial information that is prepared on different bases, the financial statements could usefully clarify that the budget and the accounting bases differ, and that the Statement of Comparison of Budget and Actual Amounts is prepared on the budget basis.

24. In those jurisdictions where budgets are prepared on the accrual basis and encompass the full set of financial statements, additional budget columns can be added to all the primary financial statements required by SLPSASs. In some jurisdictions, budgets prepared on the accrual basis may be presented in the form of only certain of the primary financial statements that comprise the full set of financial statements as specified by SLPSASs – for example, the budget may be presented as a statement of financial performance or a cash flow statement, with additional information provided in supporting schedules. In these cases, the additional budget columns can be included in the primary financial statements that are also adopted for presentation of the budget.

Level of Aggregation

25. Budget documents may provide great detail about particular activities, programs, or entities. These details are often aggregated into broad classes under common budget heads, budget classifications, or budget headings for presentation to, and approval by, the legislature or other authoritative body. The disclosure of budget and actual information consistent with those broad classes and budget heads or headings will ensure that comparisons are made at the level of legislative or other authoritative body oversight identified in the budget documents.

26. IPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, requires financial statements to provide information that meets a number of qualitative characteristics, including that the information is:
   (a) Relevant to the decision-making needs of users; and
   (b) Reliable in that the financial statements:
   (i) Represent faithfully the financial position, financial performance, and cash flows of the entity;
   (ii) Reflect the economic substance of transactions, other events, and conditions, and not merely the legal form;
   (iii) Are neutral, that is, free from bias;
   (iv) Are prudent; and
   (v) Are complete in all material respects.

27. In some cases, the detailed financial information included in approved budgets may need to be aggregated for presentation in financial statements in accordance with the requirements of this Standard. Such aggregation may be necessary to avoid information overload and to reflect relevant levels of legislative or other authoritative body oversight. Determining the level of aggregation will involve professional judgment. That judgment will be applied in the context of the objective of this Standard and the qualitative characteristics of financial reporting as outlined in paragraph 26 above and Appendix of SLPSAS 1, which summarizes the qualitative characteristics of financial reporting.

28. Additional budget information, including information about service achievements, may be presented in documents other than financial statements. A cross reference from financial statements to such documents is encouraged, particularly to link budget and actual data to nonfinancial budget data and service achievements.

Changes from Original to Final Budget

29. **An entity shall present an explanation of whether changes between the original and final budget are a consequence of reallocations within the budget, or of other factors:**

    (a) **By way of note disclosure in the financial statements; or**

    (b) **In a report issued before, at the same time as, or in conjunction with, the financial statements, and shall include a cross reference to the report in the notes to the financial statements.**

30. The final budget includes all changes approved by legislative actions or other designated authority to revise the original budget. Consistent with the requirements of this Standard, a public sector entity will include in the notes to the financial statements or in a separate report issued before, in conjunction with, or at the same time as the financial statements, an explanation of changes between the original and final budget. That explanation will include whether, for example, changes arise as a consequence of reallocations within the original budget parameters or as a consequence of other factors, such as changes in the overall budget parameters, including changes in government policy. Such disclosures are often made in a management discussion and analysis or similar report on operations issued in conjunction with, but not as part of, the financial statements. Such disclosures may also be included in budget out-turn reports issued by governments to report on budget execution. Where disclosures are made in separate reports rather than in the financial statements, the notes to the financial statements will include a cross reference to the report.

Comparable Basis

31. **All comparisons of budget and actual amounts shall be presented on a comparable basis to the budget.**

32. The comparison of budget and actual amounts will be presented on the same accounting basis (accrual, cash, or other basis), same classification basis, and for the same entities and period as for the approved budget. This will ensure that the disclosure of information about compliance with the budget in the financial statements is on the same basis as the budget itself. In some cases, this may mean presenting a budget and actual comparison on a different basis of accounting, for a different group of activities, and with a different presentation or classification format than that adopted for the financial statements.

33. Financial statements consolidate entities and activities controlled by the entity. As noted in paragraph 5, separate budgets may be approved and made publicly available for individual entities or particular activities that make up the consolidated financial statements. Where this occurs, the separate budgets may be recompiled for presentation in the financial statements in accordance with the requirements of this Standard. Where such recompilation occurs, it will not involve changes or revisions to approved budgets. This is because this Standard requires a comparison of actual amounts with the approved budget amounts.

34. Entities may adopt different bases of accounting for the preparation of their financial statements and for their approved budgets. For example, a government may adopt the accrual basis for its financial statements and the cash basis for its budget. In addition, budgets may focus on, or include information about, commitments to expend funds in the future and changes in those commitments, while the financial statements will report assets, liabilities, net assets/equity, revenues, expenses, other changes in net assets/equity, and cash flows. However, the budget entity and financial reporting entity will often be the same. Similarly, the period for which the budget is prepared and the classification basis adopted for the budget will often be reflected in financial statements. This will ensure that the accounting system records and reports financial information in a manner that facilitates the comparison of budget and actual data for management and for accountability purposes, for example, for monitoring progress of execution of the budget during the budget period and for reporting to the government, the public, and other users on a relevant and timely basis.

35. In some jurisdictions, budgets may be prepared on a cash or accrual basis consistent with a statistical reporting system that encompasses entities and activities different from those included in the financial statements. For example, budgets prepared to comply with a statistical reporting system may focus on the general government sector, and encompass only entities

fulfilling the primary or nonmarket functions of government as their major activity, while financial statements report on all activities controlled by a government, including the business activities of the government. SLPSAS 18, Disclosure of Financial Information about the General Government Sector, specifies requirements for note disclosure of financial information about the general government sector of a whole-of-government entity that adopts the accrual basis of accounting and elects to make such disclosures. In many cases, disclosures made in accordance with SLPSAS 18 will encompass the same entities, activities, and classification bases as adopted in budgets prepared consistent with the general government sector as defined in statistical reporting models. In these cases, disclosures made in accordance with SLPSAS 18 will also facilitate the disclosures required by this Standard.

36. In statistical reporting models, the general government sector may comprise national, state/provincial, and local government levels. In some jurisdictions, the national government may (a) control state/provincial and local governments, (b) consolidate those governments in its financial statements and (c) develop, and require to be made publicly available, an approved budget that encompasses all three levels of government. In these cases, the requirements of this Standard will apply to the financial statements of those national governmental entities. However, where a national government does not control state/provincial or local governments, its financial statements will not consolidate state/provincial or local governments. Rather, separate financial statements are prepared for each level of government. The requirements of this Standard will only apply to the financial statements of governmental entities when approved budgets for the entities and activities they control, or subsections thereof, are made publicly available.

Multi-year Budgets

37. Some governments and other entities approve and make publicly available multi-year budgets, rather than separate annual budgets. Conventionally, multi-year budgets comprise a series of annual budgets or annual budget targets. The approved budget for each component annual period reflects the application of the budgetary policies associated with the multi-year budget for that component period. In some cases, the multi-year budget provides for a roll forward of unused appropriations in any single year.

38. Governments and other entities with multi-year budgets may take different approaches to determining their original and final budget, depending on how their budget is passed. For example, a government may pass a biennial budget that contains two approved annual budgets, in which case an original and final approved budget for each annual period will be identifiable. If unused appropriations from the first year of the biennial budget are legally authorized to be spent in the second year, the original budget for the second-year period will be increased for these carry over amounts. In the rare cases in which a government passes a biennial or other

multi-period budget that does not specifically separate budget amounts into each annual period, judgment may be necessary in identifying which amounts are attributable to each annual period in determining annual budgets for the purposes of this Standard. For example, the original and final approved budget for the first year of a biennial period will encompass any approved capital acquisitions for the biennial period that occurred during the first year, together with the amount of the recurring revenue and expenditure items attributable to that year. The unexpended amounts from the first annual period would then be included in the original budget for the second annual period, and that budget together with any amendments thereto would form the final budget for the second year. Where multi-period budgets are adopted, entities are encouraged to provide additional note disclosure about the relationship between budget and actual amounts during the budget period.

Note Disclosures of Budgetary Basis, Period and Scope

39. **An entity shall explain in notes to the financial statements the budgetary basis and classification basis adopted in the approved budget.**

40. There may be differences between the accounting basis (cash, accrual, or some modification thereof) used in preparation and presentation of the budget and the accounting basis used in the financial statements. These differences may occur when the accounting system and the budget system compile information from different perspectives – the budget may focus on cash flows, or cash flows plus certain commitments, while the financial statements report cash flows and accrual information.

41. Formats and classification schemes adopted for presentation of the approved budget may also differ from the formats adopted for the financial statements. An approved budget may classify items on the same basis as is adopted in the financial statements, for example, by economic nature (compensation of employees, use of goods or services, etc.), or function (health, education, etc.). Alternatively, the budget may classify items by specific programs (for example, poverty reduction or control of contagious diseases) or program components linked to performance outcome objectives (for example, students graduating from tertiary education programs or surgical operations performed by hospital emergency services), which differ from classifications adopted in the financial statements. Further, a recurrent budget for ongoing operations (for example, education or health) may be approved separately from a capital budget for capital outlays (for example, infrastructure or buildings).

42. SLPSAS 1 requires entities to present, in notes to the financial statements, information about the basis of preparation of the financial statements and the significant accounting policies adopted. Disclosure of the budgetary basis and classification basis adopted for the preparation and presentation of approved budgets will assist users to better understand the relationship between the budget and accounting information disclosed in the financial statements.

43. **An entity shall disclose in notes to the financial statements the period of the approved budget.**

44. Financial statements are presented at least annually. Entities may approve budgets for an annual period or for multi-year periods. Disclosure of the period covered by the approved budget, where that period differs from the reporting period adopted for the financial statements, will assist the users of those financial statements to better understand the relationship of the budget data and budget comparison to the financial statements. Disclosure of the period covered by the approved budget, where that period is the same as the period covered by the financial statements, will also serve a useful confirmation role, particularly in jurisdictions where interim budgets and financial statements and reports are also prepared.

45. **An entity shall identify in notes to the financial statements the entities included in the approved budget.**

46. At the whole-of-government level, financial statements prepared in accordance with SLPSASs will encompass budget-dependent entities and GBEs controlled by the government. However, as noted in paragraph 35, approved budgets prepared in accordance with statistical reporting models may not encompass operations of the government that are undertaken on a commercial or market basis. Consistent with the requirements of paragraph 31, budget and actual amounts will be presented on a comparable basis. Disclosure of the entities encompassed by the budget will enable users to identify the extent to which the entity's activities are subject to an approved budget, and how the budget entity differs from the entity reflected in the financial statements.

Reconciliation of Actual Amounts on a Comparable Basis and Actual Amounts in the Financial Statements

47. **The actual amounts presented on a comparable basis to the budget in accordance with paragraph 31 shall, where the financial statements and the budget are not prepared on a comparable basis, be reconciled to the following actual amounts presented in the financial statements, identifying separately any basis, timing, and entity differences:**

    (a) **If the accrual basis is adopted for the budget, total revenues, total expenses, and net cash flows from operating activities, investing activities, and financing activities; or**

    (b) **If a basis other than the accrual basis is adopted for the budget, net cash flows from operating activities, investing activities, and financing activities.**

    The reconciliation shall be disclosed on the face of the statement of comparison of budget and actual amounts, or in the notes to the financial statements.

48. Differences between the actual amounts identified consistent with the comparable basis, and the actual amounts recognized in the financial statements, can usefully be classified into the following:

    (a) Basis differences, which occur when the approved budget is prepared on a basis other than the accounting basis. For example, where the budget is prepared on the cash basis or modified cash basis and the financial statements are prepared on the accrual basis;

    (b) Timing differences, which occur when the budget period differs from the reporting period reflected in the financial statements; and

    (c) Entity differences, which occur when the budget omits programs or entities that are part of the entity for which the financial statements are prepared.

    There may also be differences in formats and classification schemes adopted for presentation of financial statements and the budget.

49. The reconciliation required by paragraph 47 of this Standard will enable the entity to better discharge its accountability obligations, by identifying major sources of difference between the actual amounts on a budget basis and the amounts recognized in the financial statements. This Standard does not preclude reconciliation of each major total and subtotal, or each class of items, presented in a comparison of budget and actual amounts with the equivalent amounts in the financial statements.

50. For some entities adopting the same basis of accounting for preparation of both the budget documents and the financial statements, only the identification of differences between actual amounts in the budget and the equivalent amounts in the financial statements will be required. This will occur where the budget (a) is prepared for the same period, (b) encompasses the same entities, and (c) adopts the same presentation format as the financial statements. In these cases, a reconciliation is not required. For other entities adopting the same basis of accounting for the budget and the financial statements, there may be a difference in presentation format, reporting entity, or reporting period; for example, the approved budget may adopt a different classification or presentation format to the financial statements, may include only noncommercial activities of the entity, or maybe a multi-year budget. A reconciliation would be necessary where there are presentation, timing, or entity differences between the budget and the financial statements prepared on the same accounting basis.

51. For those entities using the cash basis (or a modified cash or modified accrual basis) of accounting for the presentation of the approved budget and the accrual basis for their financial statements, the major totals presented in the statement of budget and actual comparison will be reconciled to net cash flows from operating activities, net cash flows from investing activities,

and net cash flows from financing activities as presented in the cash flow statement prepared in accordance with SLPSAS 2, Cash Flow Statements.

52. **The disclosure of comparative information in respect of the previous period in accordance with the requirements of this Standard is not required.**

53. This Standard requires a comparison of budget and actual amounts to be included in the financial statements of entities that make publicly available their approved budget(s). It does not require the disclosure of a comparison of actuals of the previous period with the budget of that previous period, nor does it require that the related explanations of differences between the actuals and budget of that previous period be disclosed in the financial statements of the current period.

Effective Date

54. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1 2018, Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1 2018, it shall disclose that fact.**

55. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Illustrative Examples

These examples accompany, but are not part of, SLPSAS 15.

Statement of Comparison of Budget and Actual Amounts

For Government XX for the Year Ended December 31, 20XX Budget on Cash Basis (Classification of Payments by Functions)

Note: The budget and the accounting basis is different. This Statement of Comparison of Budget and Actual Amounts is prepared on the budget basis.

	Budgeted Amounts		**Actual Amounts on Comparable Basis**	***Difference: Final Budge and Actual**
(in rupees)	**Original**	**Final**		
RECEIPTS				
Taxation	X	X	X	X
Aid Agreements				
Sri Lanka agencies	X	X	X	X
Other Grants and Aid	X	X	X	X
Proceeds: Borrowing	X	X	X	X
Proceeds: Disposal of plant and equipment	X	X	X	X
Trading Activities	X	X	X	X
Other receipts	X	X	X	X
Total receipts	**X**	**X**	**X**	**X**
PAYMENTS				
Health	(X)	(X)	(X)	(X)
Education	(X)	(X)	(X)	(X)
Public order/safety	(X)	(X)	(X)	(X)
Social protection	(X)	(X)	(X)	(X)
Defense	(X)	(X)	(X)	(X)
Housing and community amenities	(X)	(X)	(X)	(X)
Recreational, cultural and religion	(X)	(X)	(X)	(X)
Economic affairs	(X)	(X)	(X)	(X)
Other	(X)	(X)	(X)	(X)
Total payments	(X)	(X)	(X)	(X)
NET RECEIPTS/(PAYMENTS)	**X**	**X**	**X**	**X**

* The "Difference…" column is not required. However, a comparison between actual and the original or the final budget, clearly identified as appropriate, may be included.

Additional Column Approach

For Government YY for the Year Ended December 31, 20XX Both Annual Budget And Financial Statements Adopt Accrual Basis
(Illustrated only for Statement of Financial Performance. Similar presentation would be adopted for other financial statements.)

Actual 20XX-1	(in rupees)	**Actual 20XX**	**Final Budget 20XX**	**Original Budget 20XX**	**Difference Original Budget and Actual*
	Revenue				
X	Taxes	X	X	X	X
X	Fees, fines, penalties, and licenses	X	X	X	X
X	Revenue from exchange transactions	X	X	X	X
X	Transfers from other governments	X	X	X	X
X	Other revenue	X	X	X	X
X	**Total revenue**	X	X	X	X
	Expenses				
(X)	Wages, salaries, employee benefits	(X)	(X)	(X)	(X)
(X)	Grants and other transfer payments	(X)	(X)	(X)	(X)
(X)	Supplies and consumables used	(X)	(X)	(X)	(X)
(X)	Depreciation/amortization expense	(X)	(X)	(X)	(X)
(X)	Other expenses	(X)	(X)	(X)	(X)
(X)	Finance costs	(X)	(X)	(X)	(X)
(X)	**Total expenses**	(X)	(X)	(X)	(X)
X	**Surplus/(deficit) for the period**	**X**	**X**	**X**	**X**

Extract of Note Disclosures—for Government X

(Government X presents its approved budget on a cash basis and the financial statements on the accrual basis.)

1. The budget is approved on a cash basis by functional classification. The approved budget covers the fiscal period from January 1, 20XX to December 31, 20XX, and includes all entities within the general government sector. The general government sector includes all entities identified as government departments in note xx.

2. The original budget was approved by legislative action on (date), and a supplemental appropriation of XXX for disaster relief support was approved by legislative action on (date) due to the earthquake in the Northern Region on (date). The original budget objectives and policies and subsequent revisions are explained more fully in the Operational Review and Budget Outcomes reports issued in conjunction with the financial statements.

3. The excess of actual expenditure over the final budget of 15% (25% over original budget) for the Health function was due to expenditures above the level approved by legislative action in response to the earthquake. There were no other material differences between the final approved budget and the actual amounts.

4. The budget and the accounting bases differ. The financial statements for the whole-of-government are prepared on the accrual basis, using a classification based on the nature of expenses in the statement of financial performance. The financial statements are consolidated statements that include all controlled entities, including government business enterprises for the fiscal period from January 1, 20XX to December 31, 20XX. The financial statements differ from the budget which is approved on the cash basis and which deals only with the general government sector which excludes government business enterprises and certain other non-market government entities and activities.

5. The amounts in the financial statements were recast from the accrual basis to the cash basis, and reclassified by functional classification to be on the same basis as the final approved budget. In addition, adjustments to amounts in the financial statements for timing differences associated with the continuing appropriation and differences in the entities covered (GBEs) were made to express the actual amounts on a comparable basis to the final approved budget. The amount of these adjustments are identified in the following table.

6. A reconciliation between the actual amounts on a comparable basis as presented in the Statement of Comparison of Budget and Actual Amounts and the actual amounts in the Statement of Cash Flows for the Year Ended December 31, 20XX is presented below. The financial statements and budget documents are prepared for the same period. There is an entity difference: the budget is prepared for the general government sector, and the financial statements consolidate all entities controlled by the government. There is also a basis difference: the budget is prepared on a cash basis and the financial statements on the accrual basis.

	Operating	**Financing**	**Investing**	**Total**
Actual Amount on Comparable Basis as Presented in the Budget and Actual Comparative Statement.	x	x	x	x
Basis Differences	x	x	x	x
Timing Differences	-	-	-	-
Entity Differences	x	x	x	x
Actual Amount in the Statement of Cash Flow	x	x	x	x

(This reconciliation could be included on the face of the Statement of Comparison of Budget and Actual Amounts or as a note disclosure.)

Encouraged Note Disclosure: Biennial Budget on Cash Basis - For Government B for the Year Ended December 31, 20XX

(in rupees)	**Original Biennial Budget Year**	**Target Budget for 1st Year**	**Revised Budget in 1st Year**	**1st Year Actual on Comparable Basis**	**Balance Available for 2nd Year**	**Target Budget for 2nd Year**	**Revised Budget in 2nd Year**	**2nd Year Actual on Comparable Basis**	****Difference: Budget and Actual over Budget Period***
RECEIPTS									
Taxation	X	X	X	X	X	X	X	X	X
Aid Agreements	X	X	X	X	X	X	X	X	X
Proceeds: Borrowing	X	X	X	X	X	X	X	X	X
Proceeds: Disposal of plant and equipment	X	X	X	X	X	X	X	X	X
Trading Activities									
Other receipts	X	X	X	X	X	X	X	X	X
Total receipts	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**
PAYMENTS									
Health	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Education	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Public order and safety	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Social protection	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)

(in rupees)	**Original Biennial Budget Year**	**Target Budget for 1st Year**	**Revised Budget in 1st Year**	**1st Year Actual on Comparable Basis**	**Balance Available for 2nd Year**	**Target Budget for 2nd Year**	**Revised Budget in 2nd Year**	**2nd Year Actual on Comparable Basis**	***Difference: Budget and Actual over Budget Period***
Defense	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Housing, community amenities	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Recreational, cultural, religion	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Economic affairs	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Other	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)	(X)
Total payments	**(X)**	**(X)**	**(X)**	**(X)**	**(X)**	**(X)**	**(X)**	**(X)**	**(X)**
NET RECEIPTS/ (PAYMENTS)	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**

SLPSAS – 16 – Construction Contracts

Acknowledgement

Construction Contracts (SLPSAS – 16) of the “Sri Lanka Public Sector Accounting Standards – Volume III” is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 16 - CONSTRUCTION CONTRACTS

CONTENTS

Sri Lanka Public Sector Accounting Standard 16, Construction Contracts, is set out in the objective and paragraphs 1-58. All the paragraphs have equal authority. SLPSAS 16 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

The objective of this Standard is to prescribe the accounting treatment of costs and revenue associated with construction contracts. The Standard:

- Identifies the arrangements that are to be classified as construction contracts;
- Provides guidance on the types of construction contracts that can arise in the public sector; and
- Specifies the basis for recognition and disclosure of contract expenses and, if relevant, contract revenues.

Because of the nature of the activity undertaken in construction contracts, the date at which the contract activity is entered into and the date when the activity is completed usually fall into different reporting periods.

In many jurisdictions, construction contracts entered into by public sector entities will not specify an amount of contract revenue. Rather, funding to support the construction activity will be provided by an appropriation or similar allocation of general government revenue, or by aid or grant funds. In these cases, the primary issue in accounting for construction contracts is the (a) allocation of construction costs to the reporting period in which the construction work is performed, and (b) the recognition of related expenses.

In some jurisdictions, construction contracts entered into by public sector entities may be established on a commercial basis or a noncommercial full or partial cost recovery basis. In these cases, the primary issue in accounting for construction contracts is the allocation of both contract revenue and contract costs to the reporting periods in which construction work is performed.

Scope

1. **A contractor that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for construction contracts.**
2. **This Standard applies to all public sector entities other than Government Business Enterprises.**
3. The *Preface to Sri Lanka Public Sector Accounting Standards issued* by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

Definitions

4. **The following terms are used in this Standard with the meanings specified:**

Construction contract is a contract, or a similar binding arrangement, specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology, and function or their ultimate purpose or use.
Contractor is an entity that performs construction work pursuant to a construction contract.

Cost plus or cost-based contract is a construction contract in which the contractor is reimbursed for allowable or otherwise defined costs and, in the case of a commercially based contract, an additional percentage of these costs or a fixed fee, if any.

Fixed price contract is a construction contract in which the contractor agrees to a fixed contract price, or a fixed rate per unit of output, which in some cases is subject to cost escalation clauses.
Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms published separately.*

Construction Contracts

5. A construction contract (the terms construction contract and contract are used interchangeably in the remainder of this Standard) may be negotiated for the construction of a single asset such as a bridge, building, dam, pipeline, road, ship, or tunnel. A construction contract may also deal with the construction of a number of assets that are closely interrelated or interdependent in terms of their design, technology, and function or their ultimate purpose or use – examples of such contracts include those for the construction of reticulated water supply systems, refineries, and other complex infrastructure assets.

6. For the purposes of this Standard, construction contracts include:

   (a) Contracts for the rendering of services that are directly related to the construction of the asset, for example, those for the services of project managers and architects; and

   (b) Contracts for the destruction or restoration of assets, and the restoration of the environment following the demolition of assets.

7. For the purposes of this Standard, construction contracts also include all arrangements that are binding on the parties to the arrangement, but which may not take the form of a documented contract. For example, two government departments may enter into a formal arrangement for the construction of an asset, but the arrangement may not constitute a legal contract because, in that jurisdiction, individual departments may not be separate legal entities with the power to contract. However, provided that

the arrangement confers similar rights and obligations on the parties to it as if it were in the form of a contract, it is a construction contract for the purposes of this Standard. Such binding arrangements could include (but are not limited to) a ministerial direction, a cabinet decision, a legislative direction (such as an Act of Parliament), or a memorandum of understanding.

8. Construction contracts are formulated in a number of ways that, for the purposes of this Standard, are classified as fixed price contracts and cost plus or cost-based contracts. Some commercial construction contracts may contain characteristics of both a fixed price contract and a cost plus or cost-based contract, for example in the case of a cost plus or cost-based contract with an agreed maximum price. In such circumstances, a contractor needs to consider all the conditions in paragraphs 31 and 32 in order to determine when to recognize contract revenue and expenses.

9. Cost plus and cost-based contracts encompass both commercial and noncommercial contracts. A commercial contract will specify that revenue to cover the agreed constructor's construction costs and generate a profit margin will be provided by the other parties to the contract. However, a public sector entity may also enter into a noncommercial contract to construct an asset for another entity in return for full or partial reimbursement of costs from that entity or other parties. In some cases, the cost recovery may encompass payments by the recipient entity and specific purpose construction grants or funding from other parties.

10. In many jurisdictions, where one public sector entity constructs assets for another public sector entity, the cost of construction activity is not recovered directly from the recipient. Rather, the construction activity is funded indirectly (a) by way of a general appropriation or other allocation of general government funds to the contractor, or (b) from general purpose grants from third party funding agencies or other governments. These are classified as fixed price contracts for the purpose of this Standard.

Contractor

11. A contractor is an entity that enters into a contract to build structures, construct facilities, produce goods, or render services to the specifications of another entity. The term "contractor" includes a general or prime contractor, a subcontractor to a general contractor, or a construction manager.

Combining and Segmenting Construction Contracts

12. The requirements of this Standard are usually applied separately to each construction contract. However, in certain circumstances, it is necessary to apply the Standard to the separately identifiable components of a single contract, or to a group of contracts together, in order to reflect the substance of a contract or a group of contracts.

13. **When a contract covers a number of assets, the construction of each asset shall be treated as a separate construction contract when:**

   (a) **Separate proposals have been submitted for each asset;**

   (b) **Each asset has been subject to separate negotiation, and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and**

   (c) **The costs and revenues of each asset can be identified.**

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

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

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

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

15. **A contract may provide for the construction of an additional asset at the option of the customer, or may be amended to include the construction of an additional asset. The construction of the additional asset shall be treated as a separate construction contract when:**

   (a) **The asset differs significantly in design, technology, or function from the asset or assets covered by the original contract; or**

   (b) **The price of the asset is negotiated without regard to the original contract price.**

Contract Revenue

16. **Contract revenue shall comprise:**

   (a) **The initial amount of revenue agreed in the contract; and**

   (b) **Variations in contract work, claims, and incentive payments to the extent that:**

      (i) **It is probable that they will result in revenue; and**

      (ii) **They are capable of being reliably measured**.

17. Contract revenue is measured at the fair value of the consideration received or receivable. Both the initial and ongoing measurement of contract revenue are affected by a variety of uncertainties that depend on the outcome of future events. The estimates often need to be revised as events occur and uncertainties are resolved. Where a contract is a cost plus or cost-based contract, the initial amount of revenue may not be stated in the contract. Instead, it may need to be estimated on a basis consistent with

the terms and provisions of the contract, such as by reference to expected costs over the life of the contract.

18. In addition, the amount of contract revenue may increase or decrease from one period to the next. For example:

    (a) A contractor and a customer may agree to variations or claims that increase or decrease contract revenue in a period subsequent to that in which the contract was initially agreed;

    (b) The amount of revenue agreed in a fixed price, cost plus, or cost-based contract may increase as a result of cost escalation or other clauses;

    (c) The amount of contract revenue may decrease as a result of penalties arising from delays caused by the contractor in the completion of the contract; or

    (d) When a fixed price contract involves a fixed price per unit of output, contract revenue increases or decreases as the number of units is increased or decreased.

19. A variation is an instruction by the customer for a change in the scope of the work to be performed under the contract. A variation may lead to an increase or a decrease in contract revenue. Examples of variations are changes in the specifications or design of the asset, and changes in the duration of the contract. A variation is included in contract revenue when:

    (a) It is probable that the customer will approve the variation and the amount of revenue arising from the variation; and

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

20. A claim is an amount that the contractor seeks to collect from the customer or another party as reimbursement for costs not included in the contract price. A claim may arise from, for example, customer-caused delays, errors in specifications or design, and disputed variations in contract work. The measurement of the amounts of revenue arising from claims is subject to a high level of uncertainty, and often depends on the outcome of negotiations. Therefore, claims are only included in contract revenue when:

    (a) Negotiations have reached an advanced stage, such that it is probable that the customer will accept the claim; and

    (b) The amount that it is probable will be accepted by the customer can be measured reliably.

21. Incentive payments are additional amounts paid to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when:

(a) The contract is sufficiently advanced that it is probable that the specified performance standards will be met or exceeded; and

(b) The amount of the incentive payment can be measured reliably.

22. Contractors should review all amounts relating to the construction contract that are paid directly to subcontractors by third party funding agencies, to determine whether they meet the definition of, and recognition criteria for, revenue of the contractor under the terms of the contract. Amounts meeting the definition and recognition criteria for revenue should be accounted for by the contractor in the same way as other contract revenue. Such amounts should also be recognized as contract costs (see paragraph 25). Funding agencies may include national and international aid agencies and multilateral and bilateral development banks.

Contract Costs

23. **Contract costs shall comprise:**

(a) **Costs that relate directly to the specific contract;**

(b) **Costs that are attributable to contract activity in general, and can be allocated to the contract on a systematic and rational basis; and**

(c) **Such other costs as are specifically chargeable to the customer under the terms of the contract.**

24. Costs that relate directly to a specific contract include:

(a) Site labor costs, including site supervision;

(b) Costs of materials used in construction;

(c) Depreciation of plant and equipment used on the contract;

(d) Costs of moving plant, equipment, and materials to and from the contract site;

(e) Costs of hiring plant and equipment;

(f) Costs of design and technical assistance that are directly related to the contract;

(g) The estimated costs of rectification and guarantee work, including expected warranty costs; and

(h) Claims from third parties.

These costs may be reduced by any incidental revenue that is not included in contract revenue, for example, revenue from the sale of surplus materials at the end of the contract.

25. Contractors should review all amounts relating to the construction contract paid directly by subcontractors and which are reimbursed by third party funding agencies, to determine whether they qualify as contract costs. Amounts meeting the definition of, and recognition criteria for, contract expenses should be accounted for by the contractor in the same way as other contract expenses. Amounts reimbursed by third party funding agencies that meet the definition of, and recognition criteria for, revenue should be accounted for by the contractor in the same way as other contract revenue (see paragraph 22).

26. Costs that may be attributable to contract activity in general and can be allocated to specific contracts include:

(a) Insurance;

(b) Costs of design that are not directly related to a specific contract; and

(c) Construction overheads.

Such costs are allocated using methods that (a) are systematic and rational, and (b) are applied consistently to all costs having similar characteristics. The allocation is based on the normal level of construction activity. Construction overheads include costs such as the preparation and processing of construction personnel payroll. Costs that may be attributable to contract activity in general and can be allocated to specific contracts also include borrowing costs when the contractor adopts the allowed alternative treatment in SLPSAS 4, Borrowing Costs.

27. Costs that are specifically chargeable to the customer under the terms of the contract may include some general administration costs and development costs for which reimbursement is specified in the terms of the contract.

28. Costs that cannot be attributed to contract activity or cannot be allocated to a contract are excluded from the costs of a construction contract. Such costs include:

(a) General administration costs for which reimbursement is not specified in the contract;

(b) Selling costs;

(c) Research and development costs for which reimbursement is not specified in the contract; and

(d) Depreciation of idle plant and equipment that is not used on a particular contract.

29. Contract costs include the costs attributable to a contract for the period from the date of securing the contract to the final completion of the contract. However, costs that relate directly to a contract and that are incurred in

securing the contract are also included as part of the contract costs, if they can be separately identified and measured reliably and it is probable that the contract will be obtained. When costs incurred in securing a contract are recognized as an expense in the period in which they are incurred, they are not included in contract costs when the contract is obtained in a subsequent period.

Recognition of Contract Revenue and Expenses

30. **When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract shall be recognized as revenue and expenses respectively by reference to the stage of completion of the contract activity at the reporting date. An expected deficit on a construction contract to which paragraph 44 applies shall be recognized as an expense immediately in accordance with paragraph 44.**

31. **In the case of a fixed price contract, the outcome of a construction contract can be estimated reliably when all the following conditions are satisfied:**

    (a) **Total contract revenue, if any, can be measured reliably;**

    (b) **It is probable that the economic benefits or service potential associated with the contract will flow to the entity;**

    (c) **Both the contract costs to complete the contract and the stage of contract completion at the reporting date can be measured reliably; and**

    (d) **The contract costs attributable to the contract can be clearly identified and measured reliably, so that actual contract costs incurred can be compared with prior estimates.**

32. **In the case of a cost plus or cost-based contract, the outcome of a construction contract can be estimated reliably when all the following conditions are satisfied:**

    (a) **It is probable that the economic benefits or service potential associated with the contract will flow to the entity; and**

    (b) **The contract costs attributable to the contract, whether or not specifically reimbursable, can be clearly identified and measured reliably.**

33. The recognition of revenue and expenses by reference to the stage of completion of a contract is often referred to as the percentage of completion method. Under this method, contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses, and surplus/deficit that can be attributed to the

proportion of work completed. This method provides useful information on the extent of contract activity and performance during a period.

34. Under the percentage of completion method, contract revenue is recognized as revenue in the statement of financial performance in the reporting periods in which the work is performed. Contract costs are usually recognized as an expense in the statement of financial performance in the reporting periods in which the work to which they relate is performed. However, where it is intended at inception of the contract that contract costs are to be fully recovered from the parties to the construction contract, any expected excess of total contract costs over total contract revenue for the contract is recognized as an expense immediately in accordance with paragraph 44.

35. A contractor may have incurred contract costs that relate to future activity on the contract. Such contract costs are recognized as an asset, provided it is probable that they will be recovered. Such costs represent an amount due from the customer and are often classified as contract work in progress.

36. The outcome of a construction contract can only be estimated reliably when it is probable that the economic benefits or service potential associated with the contract will flow to the entity. However, when an uncertainty arises about the collectability of an amount already included in contract revenue, and already recognized in the statement of financial performance, the uncollectable amount or the amount in respect of which recovery has ceased to be probable is recognized as an expense rather than as an adjustment of the amount of contract revenue.

37. An entity is generally able to make reliable estimates after it has agreed to a contract that establishes:

    (a) Each party's enforceable rights regarding the asset to be constructed;

    (b) The consideration, if any, to be exchanged; and

    (c) The manner and terms of settlement.

    It is also usually necessary for the entity to have an effective internal financial budgeting and reporting system. The entity reviews and, when necessary, revises the estimates of contract revenue and contract costs as the contract progresses. The need for such revisions does not necessarily indicate that the outcome of the contract cannot be estimated reliably.

38. The stage of completion of a contract may be determined in a variety of ways. The entity uses the method that measures reliably the work performed. Depending on the nature of the contract, the methods may include:

    (a) The proportion that contract costs incurred for work performed to date bear to the estimated total contract costs;

(b) Surveys of work performed; or

(c) Completion of a physical proportion of the contract work.

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

39. When the stage of completion is determined by reference to the contract costs incurred to date, only those contract costs that reflect work performed are included in costs incurred to date. Examples of contract costs that are excluded are:

(a) Contract costs that relate to future activity on the contract, such as costs of materials that have been delivered to a contract site or set aside for use in a contract, but not yet installed, used, or applied during contract performance, unless the materials have been made especially for the contract; and

(b) Payments made to subcontractors in advance of work to be performed under the subcontract.

40. **When the outcome of a construction contract cannot be estimated reliably**:

(a) **Revenue shall be recognized only to the extent of contract costs incurred that it is probable will be recoverable; and**

(b) **Contract costs shall be recognized as an expense in the period in which they are incurred**.

An expected deficit on a construction contract to which paragraph 44 applies shall be recognized as an expense immediately in accordance with paragraph 44.

41. During the early stages of a contract, it is often the case that the outcome of the contract cannot be estimated reliably. Nevertheless, it may be probable that the entity will recover the contract costs incurred. Therefore, contract revenue is recognized only to the extent of costs incurred that are expected to be recoverable. As the outcome of the contract cannot be estimated reliably, no surplus or deficit is recognized. However, even though the outcome of the contract cannot be estimated reliably, it may be probable that total contract costs will exceed total contract revenues. In such cases, any expected excess of total contract costs over total contract revenues for the contract is recognized as an expense immediately in accordance with paragraph 44.

42. Where contract costs that are to be reimbursed by parties to the contract are not probable of being recovered, they are recognized as an expense

immediately. Examples of circumstances in which the recoverability of contract costs incurred may not be probable, and in which contract costs may need to be recognized as an expense immediately, include contracts:

(a) That are not fully enforceable, that is, their validity is seriously in question;

(b) The completion of which is subject to the outcome of pending litigation or legislation;

(c) Relating to properties that are likely to be condemned or expropriated;

(d) Where the customer is unable to meet its obligations; or

(e) Where the contractor is unable to complete the contract or otherwise meet its obligations under the contract.

43. **When the uncertainties that prevented the outcome of the contract being estimated reliably no longer exist, revenue and expenses associated with the construction contract shall be recognized in accordance with paragraph 30 rather than in accordance with paragraph 40.**

Recognition of Expected Deficits

44. **In respect of construction contracts in which it is intended at inception of the contract that contract costs are to be fully recovered from the parties to the construction contract, when it is probable that total contract costs will exceed total contract revenue, the expected deficit shall be recognized as an expense immediately.**

45. Public sector entities may enter into construction contracts that specify that the revenue intended to cover the construction costs will be provided by the other parties to the contract. This may occur where, for example:

(a) Government departments and agencies that are largely dependent on appropriations or similar allocations of government revenue to fund their operations are also empowered to contract with GBE's or private sector entities for the construction of assets on a commercial or full cost recovery basis; or

(b) Government departments and agencies transact with each other on an arm's length or commercial basis as may occur under a "purchaser-provider" or similar model of government.

In these cases, an expected deficit on a construction contract is recognized immediately in accordance with paragraph 44.

46. As noted in paragraph 9, in some cases a public sector entity may enter into a construction contract for less than full cost recovery from the other parties to the contract. In these cases, funding in excess of that specified in

the construction contract will be provided from an appropriation or other allocation of government funds to the contractor, or from general purpose grants from third party funding agencies or other governments. The requirements of paragraph 44 do not apply to these construction contracts.

47. In determining the amount of any deficit under paragraph 44, total contract revenue and total contract costs may include payments made directly to subcontractors by third party funding agencies in accordance with paragraphs 22 and 25.

48. The amount of such a deficit is determined irrespective of:

(a) Whether or not work has commenced on the contract;

(b) The stage of completion of contract activity; or

(c) The amount of surpluses expected to arise on other commercial construction contracts that are not treated as a single construction contract in accordance with paragraph 14.

Changes in Estimates

49. The percentage of completion method is applied on a cumulative basis in each reporting period to the current estimates of contract revenue and contract costs. Therefore, the effect of a change in the estimate of contract revenue or contract costs, or the effect of a change in the estimate of the outcome of a contract, is accounted for as a change in accounting estimate (see SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors.) The changed estimates are used in the determination of the amount of revenue and expenses recognized in the statement of financial performance in the period in which the change is made and in subsequent periods.

Disclosure

50. **An entity shall disclose:**

(a) **The amount of contract revenue recognized as revenue in the period;**

(b) **The methods used to determine the contract revenue recognized in the period; and**

(c) **The methods used to determine the stage of completion of contracts in progress.**

51. **An entity shall disclose each of the following for contracts in progress at the reporting date:**

(a) **The aggregate amount of costs incurred and recognized surpluses (less recognized deficits) to date;**

(b) **The amount of advances received; and**

(c) **The amount of retentions.**

52. Retentions are amounts of progress billings that are not paid until the satisfaction of conditions specified in the contract for the payment of such amounts, or until defects have been rectified. Progress billings are amounts of contract revenue billed for work performed on a contract, whether or not they have been paid by the customer. Advances are amounts of contract revenue received by the contractor before the related work is performed.

53. **An entity shall present:**

(a) **The gross amount due from customers for contract work as an asset; and**

(b) **The gross amount due to customers for contract work as a liability.**

54. The gross amount due from customers for contract work is the net amount of:

(a) Costs incurred plus recognized surpluses; less

(b) The sum of recognized deficits and progress billings for all contracts in progress for which costs incurred plus recognized surpluses to be recovered by way of contract revenue (less recognized deficits) exceed progress billings.

55. The gross amount due to customers for contract work is the net amount of:

(a) Costs incurred plus recognized surpluses; less

(b) The sum of recognized deficits and progress billings for all contracts in progress for which progress billings exceed costs incurred plus recognized surpluses to be recovered by way of contract revenue (less recognized deficits).

56. Guidance on the disclosure of contingent liabilities and contingent assets can be found in SLPSAS 8, Provisions, Contingent Liabilities and Contingent Assets. Contingent liabilities and contingent assets may arise from such items as warranty costs, claims, penalties, or possible losses.

Effective Date

57. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1 2018, Earlier**

application is encouraged. If an entity applies this Standard for a period beginning before January 1 2018, it shall disclose that fact.

58. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Implementation Guidance

This guidance accompanies, but is not part of, SLPSAS 16.

Disclosure of Accounting Policies

IG1. The following are examples of accounting policy disclosures for a department that enters noncommercial construction contracts with other government agencies for full, partial, or no cost recovery from the other parties to the contract. The department is also empowered to enter into commercial construction contracts with private sector entities and GBEs, and to enter full cost recovery construction contracts with certain state hospitals and state universities.

Noncommercial Contracts

IG2. Contract costs are recognized as an expense on the percentage of completion method, measured by reference to the percentage of labor hours incurred to date to estimated total labor hours for each contract. In some cases, certain construction activity and technical supervision have been subcontracted to private sector contractors for a fixed "completion of contract" fee. Where this has occurred, the subcontracted costs are recognized as an expense on the percentage of completion method for each subcontract.

IG3. Contract revenue from full cost recovery contracts and partial cost recovery contracts entered into by the Department is recognized by reference to the recoverable costs incurred during the period, measured by the proportion that recoverable costs incurred to date bear to the estimated total recoverable costs of the contract.

Commercial Contracts

IG4. Revenue from fixed price construction contracts is recognized on the percentage of completion method, measured by reference to the percentage of labor hours incurred to date to estimated total labor hours for each contract.

IG5. Revenue from cost plus or cost-based contracts is recognized by reference to the recoverable costs incurred during the period plus the fee earned, measured by the proportion that costs incurred to date bear to the estimated total costs of the contract.

The Determination of Contract Revenue and Expenses

IG6. The following examples deal with a noncommercial and a commercial construction contract. The examples illustrate one method of determining the stage of completion of a contract and the timing of the recognition of contract revenue and expenses (see paragraphs 30–43 of this Standard).

Noncommercial Contracts

IG7. The Department of Works and Services (the construction contractor) has a contract to build a bridge for the Department of Roads and Highways. The Department of Works and Services is funded by appropriation. The construction contract identifies construction requirements, including anticipated costs, technical specifications, and timing of completion, but does not provide for any recovery of construction costs directly from the Department of Roads and Highways. The construction contract is a key management planning and accountability document attesting to the design and construction qualities of the bridge. It is used as input in assessing the performance of the contracting parties in delivering services of agreed technical specification within projected cost parameters. It is also used as input to future cost projections.

IG8. The initial estimate of contract costs is 8,000. It will take three years to build the bridge. An aid agency has agreed to provide funding of 4,000, being half of the construction costs – this is specified in the construction contract.

IG9. By the end of Year 1, the estimate of contract costs has increased to 8,050. The aid agency agrees to fund half of this increase in estimated costs.

IG10. In Year 2, the Government on the advice of the Department of Roads and Highways approves a variation resulting in estimated additional contract costs of 150. The aid agency agrees to fund 50% of this variation. At the end of Year 2, costs incurred include 100 for standard materials stored at the site to be used in Year 3 to complete the project.

IG11. The Department of Works and Services determines the stage of completion of the contract by calculating the proportion that contract costs incurred for work performed to date bear to the latest estimated total contract costs.

IG12. A summary of the financial data during the construction period is as follows:

	Year 1	**Year 2**	**Year 3**
Initial amount of revenue agreed in contract	4,000	4,000	4,000
Variation	–	100	100
Total Contract Revenue	4,000	4,100	4,100
Contract costs incurred to date	2,093	6,168	8,200
Contract costs to complete	5,957	2,032	-
Total estimated contract costs	8,050	8,200	8,200
Stage of completion	26%	74%	100%

IG13. The stage of completion for Year 2 (74%) is determined by excluding from contract costs incurred for work performed to date the 100 for standard materials stored at the site for use in Year 3.

IG14. The amounts of contract revenue and expenses recognized in the statement of financial performance in the three years are as follows:

	To Date	Recognized in prior years	Recognized in current year
Year 1			
Revenue (4,000 × .26)	1,040		1,040
Expenses (8,050 × .26)	2,093		2,093
Year 2			
Revenue (4,100 × .74)	3,034	1,040	1,994
Expenses (8,200 × .74)	6,068	2,093	3,975
Year 3			
Revenue (4,100 × 1.00)	4,100	3,034	1,066
Expenses (8,200 × 1.00)	8,200	6,068	2,132

Commercial Contracts

IG15. The Department of Works and Services (the contractor), while predominantly funded by appropriation, is empowered to undertake limited construction work on a commercial basis for private sector entities. With the authority of the Minister, the Department has entered a fixed price commercial contract for 9,000 to build a bridge.

IG16. The initial amount of revenue agreed in the contract is 9,000. The contractor's initial estimate of contract costs is 8,000. It will take three years to build the bridge.

IG17. By the end of Year 1, the Department's estimate of contract costs has increased to 8,050.

IG18. In Year 2, the customer approves a variation resulting in an increase in contract revenue of 200 and estimated additional contract costs of 150. At the end of Year 2, costs incurred include 100 for standard materials stored at the site to be used in Year 3 to complete the project.

IG19. The Department determines the stage of completion of the contract by calculating the proportion that contract costs incurred for work performed to date bear to the latest estimated total contract costs. A summary of the financial data during the construction period is as follows:

	Year 1	**Year 2**	**Year 3**
Initial amount of revenue agreed in contract	9,000	9,000	9,000
Variation	–	200	200
Total Contract Revenue	9,000	9,200	9,200
Contract costs incurred to date	2,093	6,168	8,200
Contract costs to complete	5,957	2,032	–
Total estimated contract costs	8,050	8,200	8,200
Estimated surplus	950	1,000	1,000
Stage of completion	26%	74%	100%

IG20. The stage of completion for Year 2 (74%) is determined by excluding from contract costs incurred for work performed to date the 100 for standard materials stored at the site for use in Year 3.

IG21. The amounts of revenue, expenses, and surplus recognized in the statement of financial performance in the three years are as follows:

	To Date	**Recognized in prior years**	**Recognized in current year**
Year 1			
Revenue (9,000 × .26)	2,340		2,340
Expenses (8,050 × .26)	2,093		2,093
Surplus	247		247
Year 2			
Revenue (9,200 × .74)	6,808	2,340	4,468
Expenses (8,200 × .74)	6,068	2,093	3,975
Surplus	740	247	493
Year 3			
Revenue (9,200× 1.00)	9,200	6,808	2,392
Expenses (8,200 × 1.00)	8,200	6,068	2,132
Surplus	1,000	740	260

Contract Disclosures

Appropriation/Aid Funded Contracts and Full Cost Recovery Contracts

IG22. The Department of Works and Services was recently created as the entity to manage the construction of major buildings and roadworks for other government entities. It is funded predominantly by appropriation, but with the approval of the Minister is empowered to undertake construction projects financed by national or international aid agencies. It has its own construction capabilities and can also subcontract. With the approval of the Minister, the Department may also undertake construction work on a commercial basis for private sector entities and GBEs and on a full cost recovery basis for state hospitals and state run universities.

IG23. The Department of Works and Services has reached the end of its first year of operations. All its contract costs incurred have been paid for in cash, and all its progress billings (to aid agencies that have commissioned construction work) have been received in cash. No advances to the Department for construction work were made during the period. Contract costs incurred for contracts B and C include the cost of materials that have been purchased for the contract but which have not been used in contract performance to date. No commercial contracts have been undertaken this year. (See below for examples of commercial contracts.)

- Contract A is funded out of general appropriation revenue. (The contract includes no "contract revenue" as defined.)
- Contract B is with the Department of Education and the XX Aid Agency, which is funding 50% of the construction costs. (50% of the contract cost is to be reimbursed by parties to the contract and therefore is "contract revenue" as defined.)
- Contract C is totally funded by the National University. (The terms of the arrangement specify that all of the contract costs are to be reimbursed by the National University from the University's major construction fund. Therefore, "contract revenue" as defined equals contract costs.)

IG24. The status of the three contracts in progress at the end of Year 1 is as follows:

	Contract			
	A	B	C	Total
Contract Revenue recognized in accordance with paragraph 30	_	225	350	575
Contract Expenses recognized in accordance with paragraph 30	110	450	350	910
Contract Costs funded by Appropriation	110	225	–	335
Contract Costs incurred in the period	110	510	450	1,070
– recognized as expenses (para 30)	110	450	350	910
– recognized as an asset (para 35)		60	100	160
Contract Revenue (see above)	–	225	350	575
Progress Billings (para 52)	–	225	330	555
Unbilled Contract Revenue	–	–	20	20
Advances (para 52)	–	–	–	–

The amounts to be disclosed in accordance with the standard are as follows:

Contract revenue recognized as revenue in the period (para 50(a))	575
Contract costs incurred to date (para 51(a)) (there are no recognized surpluses/less recognized deficits)	1,070
Gross amount due from contract customers for contract work (determined in accordance with paragraph 54 and presented as an asset in accordance with paragraph 53(a))	150

The amounts to be disclosed in accordance with the

standard are as follows:

Contract revenue recognized as revenue in the period (para 50(a))	575
Contract costs incurred to date (para 51(a)) (there are no recognized surpluses/less recognized deficits)	1,070
Gross amount due from contract customers for contract work (determined in accordance with paragraph 54 and presented as an asset in accordance with paragraph 53(a))	150

Amounts to be disclosed in accordance with paragraphs 51(a) and 53(a) are as follows (Note: contract revenue for B is 50% of contract costs):

	A	**B**	**C**	**Total**
Contract costs incurred	110	510	450	1,070
Progress billings	0	225	330	555
Due from aid agencies and customers	–	30	120	150

IG25. The amount disclosed in accordance with paragraph 51(a) is the same as the amount for the current period because the disclosures relate to the first year of operation.

Commercial Contracts

IG26. The Division of National Construction Works has been established within the Department of Works and Services to undertake construction work on a commercial basis for GBEs and private sector entities at the direction, and with the approval, of the Minister. The Division has reached the end of its first year of operations. All its contract costs incurred have been paid for in cash, and all its progress billings and advances have been received in cash. Contract costs incurred for contracts B, C, and E include the cost of materials that have been purchased for the contract, but which have not been used in contract performance to date. For contracts B, C, and E, the customers have made advances to the contractor for work not yet performed.

IG27. The status of its five contracts in progress at the end of Year 1 is as follows:

	Contract					
	A	**B**	**C**	**D**	**E**	**Total**
Contract revenue recognized in accordance with paragraph 30	145	520	380	200	55	1,300
Contract expenses recognized in accordance with paragraph 30	110	450	350	250	55	1,215
Expected deficits recognized in accordance with paragraph 44	–	–	–	40	30	70
Recognized surpluses less recognized deficits	35	70	30	(90)	(30)	15

Contract costs incurred in the period	110	510	450	250	100	1,420
Contract costs incurred recognized as contract expenses in the period in accordance with paragraph 30	110	450	350	250	55	1,215
Contract costs that relate to future activity recognized as an asset in accordance with paragraph 35	–	60	100	–	45	205
Contract revenue (see above)	145	520	380	200	55	1,300
Progress billings (para 52)	100	520	380	180	55	1,235
Unbilled contract Revenue	45	–	–	20	–	65
Advances (para 52)	–	80	20	–	25	125

The amounts to be disclosed in accordance with the Standard are as follows: Contract revenue recognized as revenue in the period (para 50(a))	1,300
Contract costs incurred and recognized surpluses (less recognized deficits) to date (para 51(a))	1,435
Advances received (para 51(b))	125
Gross amount due from customers for contract work – presented as an asset in accordance with paragraph 53(a)	220
Gross amount due to customers for contract work – presented as an asset in accordance with paragraph 53(b)	(20)

The amounts to be disclosed in accordance with paragraphs 51(a), 53(a), and 53(b) are calculated as follows:

	A	**B**	**C**	**D**	**E**	**Total**
Contract costs incurred	110	510	450	250	100	1,420
Recognized surpluses less recognized deficits	35	70	30	(90)	(30)	15
	145	580	480	160	70	1,435
Progress billings	100	520	380	180	55	1,235
Due from customers	45	60	100	–	15	220
Due to customers	–	–	–	(20)	–	(20)

IG28. The amount disclosed in accordance with paragraph 51(a) is the same as the amount for the current period because the disclosures relate to the first year of operation.

SLPSAS – 17 – Segment Reporting

Acknowledgement

Segment Reporting (SLPSAS – 17) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 17 - SEGMENT REPORTING
CONTENTS

Sri Lanka Public Sector Accounting Standard 17, Segment Reporting, is set out in the objective and paragraphs 1-77. All the paragraphs have equal authority. SLPSAS 17 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

The objective of this Standard is to establish principles for reporting financial information by segments. The disclosure of this information will:

(a) Help users of the financial statements to better understand the entity's past performance, and to identify the resources allocated to support the major activities of the entity; and

(b) Enhance the transparency of financial reporting and enable the entity to better discharge its accountability obligations.

Scope

1. An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in the presentation of segment information.

2. This Standard applies to all public sector entities other than Government Business Enterprises.

3. The Preface to Sri Lanka Public Sector Accounting Standards issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, Presentation of Financial Statements.

4. **This Standard shall be applied in complete sets of published financial statements that comply with SLPSASs.**

5. A complete set of financial statements includes a statement of financial position, statement of financial performance, cash flow statement, a statement showing changes in net assets/equity, and notes, as provided in SLPSAS 1.

6. **If both consolidated financial statements of a government or other economic entity and the separate financial statements of the parent entity are presented together, segment information need be presented only on the basis of the consolidated financial statements.**

7. In some jurisdictions, the consolidated financial statements of the government or other economic entity and the separate financial statements of the controlling entity are compiled and presented together in a single report. Where this occurs, the report that contains the government's or other controlling entity's consolidated financial statements needs to present segment information only for the consolidated financial statements.

Definitions

8. [Not used to maintain consistency of paragraph numbers with IPSASs]

9. **The following term is used in this Standard with the meaning specified:**
A segment is a distinguishable activity or group of activities of an entity for which it is appropriate to separately report financial information for the purpose of (a) evaluating the entity's past performance in achieving its objectives, and (b) making decisions about the future allocation of resources.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms* published separately.

10. Governments and their agencies control significant public resources, and operate to provide a wide variety of goods and services to their constituents in differing geographical regions and in regions with differing socioeconomic characteristics. These entities are expected, and in some cases formally required, to use those resources efficiently and effectively to achieve the entity's objectives. Entity-wide and consolidated financial statements provide an overview of (a) the assets controlled and liabilities incurred by the reporting entity, (b) the cost of services provided, and (c) the taxation revenue, budget allocations, and cost recoveries generated to fund the provision of those services. However, this aggregate information does not provide information about the specific operational objectives and major activities of the reporting entity and the resources devoted to, and costs of, those objectives and activities.

11. In most cases, the activities of the entity are so broad, and encompass so wide a range of different geographical regions, or regions with different socio-economic characteristics, that it is necessary to report disaggregated financial and non-financial information about particular segments of the entity to provide relevant information for accountability and decision making purposes.

Reporting by Segments

12. An entity shall identify its separate segments in accordance with the requirements of paragraph 9 of this Standard, and shall present information about those segments as required by paragraphs 51–75 of this Standard.

13. Under this Standard, public sector entities will identify as separate segments each distinguishable activity or group of activities for which financial information should be reported, for purposes of (a) evaluating the past performance of the entity in achieving its objectives, and (b) making decisions about the allocation of resources by the entity. In addition to disclosure of the information required by paragraphs 51–75 of this Standard, entities are also encouraged to disclose additional information about reported segments as identified by this Standard or as considered necessary for accountability and decision-making purposes.

Reporting Structures

14. In most cases, the major classifications of activities identified in budget documentation will reflect the segments for which information is reported to the governing body and the most senior manager of the entity. In most cases, the segments reported to the governing body and senior manager will also reflect the segments reported in the financial statements. This is because the governing board and senior manager will require information about segments to enable them (a) to discharge their managerial responsibilities and to evaluate the performance of the entity in achieving its objectives in the past, and (b) to make decisions about the allocation of resources by the entity in the future.

15. Determining the activities that should be grouped as separate segments and reported in the financial statements for accountability and decision-making purposes involves judgment. In making that judgment, preparers of the financial statements will consider such matters as:

    (a) The objective of reporting financial information by segment as identified in paragraph 9 above;

    (b) The expectations of members of the community and their elected or appointed representatives regarding the key activities of the entity;

    (c) The qualitative characteristics of financial reporting as identified in Appendix A of SLPSAS 1. These characteristics are also summarized in the Implementation Guidance to this standard. They include the relevance, reliability, and comparability over time of financial information that is reported about an entity's different segments. (these characteristics are based on the qualitative characteristics of financial statements identified in the CA Sri Lanka Framework for the *Preparation and Presentation of Financial Statements);* and

    (d) Whether a particular segment structure reflects the basis on which the governing body and senior manager require financial information to enable them to assess the past performance of the entity in achieving its objectives, and to make decisions about the allocation of resources to achieve entity objectives in the future.

16. At the whole-of-government level, financial information is often aggregated and reported in a manner that reflects, for example:

    (a) Major economic classifications of activities undertaken by general government, such as health, education, defense, and welfare (these may reflect the Government Finance Statistics (GFS) functional classifications of government), and major trading activities undertaken by GBEs, such as state-owned power stations, banks, and insurance entities; or

    (b) Portfolio responsibilities of individual ministers or members of executive government. These often, but not always, reflect the economic classifications in (a) above – differences may occur because portfolio responsibilities may aggregate more than one of the economic classifications or cut across those classifications.

Service Segments and Geographical Segments

17. The types of segments reported to the governing body and senior manager of an entity are frequently referred to as service segments or geographical segments. These terms are used in this Standard with the following meanings:

    (a) A service segment refers to a distinguishable component of an entity that is engaged in providing related outputs or achieving particular operating objectives consistent with the overall mission of each entity; and

    (b) A geographical segment is a distinguishable component of an entity that is engaged in providing outputs or achieving particular operating objectives within a particular geographical area.

18. Government departments and agencies are usually managed along service lines, because this reflects the way in which (a) major outputs are identified, (b) their achievements monitored, and (c) their resource needs identified and budgeted. An example of an entity that reports internally on the basis of service lines or service segments is an education department whose organizational structure and internal reporting system reflects primary, secondary, and tertiary educational activities and outputs as separate segments. This basis of segmentation may be adopted internally, because the skills and facilities necessary to deliver the desired outputs and outcomes for each of these broad educational activities are perceived to be different. In addition, key financial decisions faced by management include determination of the resources to allocate to each of those outputs or activities. In these cases, it is likely that reporting externally on the basis of service segments will also satisfy the requirements of this Standard.

19. Factors that will be considered in determining whether outputs (goods and services) are related and should be grouped as segments for financial reporting purposes include:

    (a) The primary operating objectives of the entity and the goods, services, and activities that relate to the achievement of each of those objectives, and whether resources are allocated and budgeted on the basis of groups of goods and services;

    (b) The nature of the goods or services provided or activities undertaken;

    (c) The nature of the production process and/or service delivery and distribution process or mechanism;

(d) The type of customer or consumer for the goods or services;

(e) Whether this reflects the way in which the entity is managed and financial information is reported to senior management and the governing board; and

(f) If applicable, the nature of the regulatory environment, (for example, department or statutory authority) or sector of government (for example finance sector, public utilities, or general government).

20. An entity may be organized and report internally to the governing body and the senior manager on a regional basis – whether within or across national, state, local, or other jurisdictional boundaries. Where this occurs, the internal reporting system reflects a geographical segment structure.

21. A geographical segment structure may be adopted where, for example, the organizational structure and internal reporting system of an education department is structured on the basis of regional educational outcomes, because the key performance assessments and resource allocation decisions to be made by the governing body and senior manager are determined by reference to regional achievements and regional needs. This structure may have been adopted to preserve regional autonomy of educational needs and delivery of education services, or because operating conditions or educational objectives are substantially different from one region to another. It may also have been adopted simply because management believes that an organizational structure based on regional devolution of responsibility better serves the objectives of the organization. In these cases, resource allocation decisions are initially made, and subsequently monitored, by the governing body and the senior manager on a regional basis. Detailed decisions about the allocation of resources to particular functional activities within a geographical region are then made by regional management, consistent with educational needs within that region. In these cases, it is likely that reporting information by geographical segments in the financial statements will also satisfy the requirements of this Standard.

22. Factors that will be considered in determining whether financial information should be reported on a geographical basis include:

(a) Similarity of economic, social, and political conditions in different regions;

(b) Relationships between the primary objectives of the entity and the different regions;

(c) Whether service delivery characteristics and operating conditions differ in different regions;

(d) Whether this reflects the way in which the entity is managed and financial information is reported to senior managers and the governing board; and

(e) Special needs, skills, or risks associated with operations in a particular area.

Multiple Segmentation

23. In some cases, an entity may report to the governing body and senior manager segment revenue, expense, assets, and liabilities on the basis of more than one segment structure, for example by both service and geographical segments. Reporting on the basis of both service segments and geographical segments in the external financial statements often will provide useful information if the achievement of an entity's objectives is strongly affected both by the different products and services it provides and the different geographical areas to which those goods and services are provided. Similarly, at the whole-of-government level, a government may adopt a basis of disclosure that (a) reflects general government, public finance sector and trading sector disclosures, and (b) supplements the general government sector analysis with, for example, segment disclosures of major purpose or functional sub-categories. In these cases, the segments may be reported separately or as a matrix. In addition, a primary and secondary segment reporting structure may be adopted with only limited disclosures made about secondary segments.

Reporting Structures not Appropriate

24. As noted above, in most cases the segments for which information is reported internally to the governing body and the most senior manager of the entity, for the purpose of evaluating the entity's past performance and for making decisions about the future allocation of resources, will reflect those identified in budget documentation and will also be adopted for external reporting purposes in accordance with the requirements of this Standard. However, in some cases an entity's internal reporting to the governing body and the senior manager may be structured to aggregate and report on a basis that distinguishes revenues, expenses, assets, and liabilities related to budget-dependent activities from those of trading activities, or which distinguishes budget-dependent entities from GBEs. Reporting segment information in the financial statements on the basis of only these segments is unlikely to meet the objectives specified for this Standard. This is because these segments are unlikely to provide information that is relevant to users about, for example, the performance of the entity in achieving its major operating objectives. SLPSAS 18, Disclosure of Financial Information about the General Government Sector, includes requirements for governments that elect to disclose financial information about the general government sector (GGS) as defined in statistical bases of reporting.

25. In some cases, the disaggregated financial information reported to the governing body and the senior manager may not report expenses, revenues, assets, and liabilities by service segment, geographical segment, or by reference to other activities. Such reports may be constructed to reflect only expenditures by nature (for example, wages, rent, supplies, and capital acquisitions) on a line item basis that is consistent with the budget appropriation or other funding or expenditure authorization model applicable to the entity. This may occur where the purpose of financial reporting to the governing body and senior management is to evidence compliance with spending mandates rather than for purposes of (a) evaluating the past performance of the entity's major activities in achieving their objectives, and (b) making decisions about the future allocation of resources. When internal reporting to the governing body and senior manager is structured to report only compliance information, reporting externally on the same basis as the internal reporting to the governing body and senior manager will not meet the requirement of this Standard.

26. When an entity's internal reporting structure does not reflect the requirements of this Standard, for external reporting purposes the entity will need to identify segments that satisfy the definition of a segment in paragraph 9 and disclose the information required by paragraphs 51–75.

Definitions of Segment Revenue, Expense, Assets, Liabilities, and Accounting Policies

27. **The following additional terms are used in this Standard with the meanings specified:**

<u>Segment accounting policies</u> are the accounting policies adopted for preparing and presenting the financial statements of the consolidated group or entity as well as those accounting policies that relate specifically to segment reporting.

<u>Segment assets</u> are those operating assets that are employed by a segment in its operating activities, and that either are directly attributable to the segment or can be allocated to the segment on a reasonable basis.

If a segment's segment revenue includes interest or dividend revenue, its segment assets include the related receivables, loans, investments, or other revenue-producing assets.

Segment assets do not include income tax or income tax-equivalent assets that are recognized in accordance with accounting standards dealing with obligations to pay income tax or income tax equivalents.

Segment assets include investments accounted for under the equity method only if the net surplus (deficit) from such investments is included in segment revenue.

Segment assets are determined after deducting related allowances that are reported as direct offsets in the entity's statement of financial position.

Segment expense is an expense resulting from the operating activities of a segment that is directly attributable to the segment, and the relevant portion of an expense that can be allocated on a reasonable basis to the segment, including expenses relating to the provision of goods and services to external parties and expenses relating to transactions with other segments of the same entity. Segment expense does not include:

(a) Interest, including interest incurred on advances or loans from other segments, unless the segment's operations are primarily of a financial nature;

(b) Losses on sales of investments or losses on extinguishment of debt, unless the segment's operations are primarily of a financial nature;

(c) An entity's share of net deficit or losses of associates, joint ventures, or other investments accounted for under the equity method;

(d) Income tax or income tax-equivalent expense that is recognized in accordance with accounting standards dealing with obligations to pay income tax or income tax equivalents; or

(e) General administrative expenses, head office expenses, and other expenses that arise at the entity level and relate to the entity as a whole. However, costs are sometimes incurred at the entity level on behalf of a segment. Such costs are segment expenses if they relate to the segment's operating activities and they can be directly attributed or allocated to the segment on a reasonable basis.

For a segment's operations that are primarily of a financial nature, interest revenue and interest expense may be reported as a single net amount for segment reporting purposes only if those items are netted in the consolidated or entity financial statements.

Segment liabilities are those operating liabilities that result from the operating activities of a segment, and that either are directly attributable to the segment or can be allocated to the segment on a reasonable basis.

If a segment's segment expense includes interest expense, its segment liabilities include the related interest-bearing liabilities.

Segment liabilities do not include income tax or income tax equivalent liabilities that are recognized in accordance with accounting standards dealing with obligations to pay income tax or income tax equivalents.

Segment revenue is revenue reported in the entity's statement of financial performance that is directly attributable to a segment, and the relevant portion of entity revenue that can be allocated on a reasonable basis to a segment, whether from budget appropriations or similar, grants, transfers, fines, fees, or sales to external customers or from transactions with other segments of the same entity. Segment revenue does not include:

(a) Interest or dividend revenue, including interest earned on advances or loans to other segments, unless the segment's operations are primarily of a financial nature; or

(b) Gains on sales of investments or gains on extinguishment of debt, unless the segment's operations are primarily of a financial nature.

Segment revenue includes an entity's share of net surplus (deficit) of associates, joint ventures, or other investments accounted for under the equity method, only if those items are included in consolidated or total entity revenue.

Attributing Items to Segments

28. The definitions of segment revenue, segment expense, segment assets, and segment liabilities include amounts of such items that are directly attributable to a segment, and amounts of such items that can be allocated to a segment on a reasonable basis.

29. An entity looks to its internal financial reporting system as the starting point for identifying those items that can be directly attributed, or reasonably allocated, to segments. That is, where segments used for internal reporting purposes are adopted, or form the basis of segments adopted, for general purpose financial statements, there is a presumption that amounts that have been identified with segments for internal financial reporting purposes are directly attributable or reasonably allocable to segments for the purpose of measuring the segment revenue, segment expense, segment assets, and segment liabilities.

30. In some cases, a revenue, expense, asset, or liability may have been allocated to segments for internal financial reporting purposes on a basis that is understood by entity management, but that could be deemed subjective, arbitrary, or difficult to understand by external users of financial statements. Such an allocation would not constitute a reasonable basis under the definitions of segment revenue, segment expense, segment assets, and segment liabilities in this Standard. Conversely, an entity may choose not to

allocate some item of revenue, expense, asset, or liability for internal financial reporting purposes, even though a reasonable basis for doing so exists. Such an item is allocated pursuant to the definitions of segment revenue, segment expense, segment assets, and segment liabilities in this Standard.

31. Public sector entities can generally identify (a) the costs of providing certain groups of goods and services or of undertaking certain activities, and (b) the assets that are necessary to facilitate those activities. This information is needed for planning and control purposes. However, in many cases the operations of government agencies and other public sector entities are funded by "block" appropriations, or appropriations on a "line item" basis reflecting the nature of the major classes of expenses or expenditures. These "block" or "line item" appropriations may not be related to specific service lines, functional activities, or geographical regions. In some cases, it may not be possible to directly attribute revenue to a segment or to allocate it to a segment on a reasonable basis. Similarly, some assets, expenses, and liabilities may not be able to be directly attributed, or allocated on a reasonable basis, to individual segments, because they support a wide range of service delivery activities across a number of segments or are directly related to general administration activities that are not identified as a separate segment. The unattributed or unallocated revenue, expense, assets, and liabilities would be reported as an unallocated amount in reconciling the segment disclosures to the aggregate entity revenue as required by paragraph 64 of this Standard.

32. Governments and their agencies may enter into arrangements with private sector entities for the delivery of goods and services, or to conduct other activities. In some jurisdictions, these arrangements take the form of a joint venture or an investment in an associate that is accounted for by the equity method of accounting. Where this is the case, segment revenue will include the segment's share of the equity accounted net surplus (deficit), where the equity accounted surplus (deficit) is included in entity revenue, and it can be directly attributed or reliably allocated to the segment on a reasonable basis.

Segment Assets, Liabilities, Revenue, and Expense

33. Examples of segment assets include current assets that are used in the operating activities of the segment: property, plant, and equipment; assets that are the subject of finance leases; and intangible assets. If a particular item of depreciation or amortization is included in segment expense, the related asset is also included in segment assets. Segment assets do not include assets used for general entity or head office purposes. For example:

    (a) The office of the central administration and policy development unit of a department of education is not included in segments reflecting the delivery of primary, secondary and tertiary educational services; or

(b) The parliamentary or other general assembly building is not included in segments reflecting major functional activities such as education, health, and defense when reporting at the whole-of-government level.

Segment assets include operating assets shared by two or more segments if a reasonable basis for allocation exists.

34. The consolidated financial statements of a government or other entity may encompass entities acquired in an entity acquisition that gives rise to purchased goodwill (guidance on accounting for the acquisition of an entity is included in SLFRS 3, Business Combinations.) In these cases, segment assets will include goodwill that is directly attributable to a segment or that can be allocated to a segment on a reasonable basis, and segment expense includes related amortization of goodwill.

35. Examples of segment liabilities include trade and other payables, accrued liabilities, advances from members of the community for the provision of partially subsidized goods and services in the future, product warranty provisions arising from any commercial activities of the entity, and other claims relating to the provision of goods and services. Segment liabilities do not include borrowings, liabilities related to assets that are the subject of finance leases, and other liabilities that are incurred for financing rather than operating purposes. If interest expense is included in segment expense, the related interest-bearing liability is included in segment liabilities.

36. The liabilities of segments whose operations are not primarily of a financial nature do not include borrowings and similar liabilities, because segment revenues and expenses do not include financing revenues and expenses. Further, because debt is often issued at the head office level or by a central borrowing authority on an entity-wide or government-wide basis, it is often not possible to directly attribute, or reasonably allocate, the interest-bearing liability to the segment. However, if the financing activities of the entity are identified as a separate segment, as may occur at the whole-of-government level, expenses of the "finance" segment will include interest expense, and the related interest-bearing liabilities will be included in segment liabilities.

37. Sri Lanka Accounting Standards may require adjustments to be made to the carrying amounts of the identifiable assets and liabilities of an entity acquired in an acquisition (see for example SLFRS 3). Measurements of segment assets and liabilities include any adjustments to the prior carrying amounts of the identifiable segment assets and segment liabilities of an entity acquired in an entity combination accounted for as a purchase, even if those adjustments are made only for the purpose of preparing consolidated financial statements and are not recorded in either the controlling entity's separate or the controlled entity's individual financial statements. Similarly, if property, plant, and equipment has been revalued subsequent to acquisition in accordance with the revaluation model in

SLPSAS 7, *Property*, *Plant*, *and Equipment*, measurements of segment assets reflect those revaluations.

38. In some jurisdictions, a government or government entity may control a GBE or other entity that operates on a commercial basis and is subject to income tax or income tax equivalents. These entities may be required to apply accounting standards such as LKAS 12, *Income Taxes*, which prescribe the accounting treatment of income taxes or income tax equivalents. Such standards may require the recognition of income tax assets and liabilities in respect of income tax expenses, or income tax-equivalent expenses, which are recognized in the current period and are recoverable or repayable in future periods. These assets and liabilities are not included in segment assets or segment liabilities because they arise as a result of all the activities of the entity as a whole and the tax arrangements in place in respect of the entity. However, assets representing taxation revenue receivable that is controlled by a taxing authority will be included in segment assets of the authority if they can be directly attributed to that segment or allocated to it on a reliable basis.

39. Some guidance for cost allocation can be found in other SLPSASs. For example, SLPSAS 9, *Inventories*, provides guidance for attributing and allocating costs to inventories, and SLPSAS 16, *Construction Contracts*, provides guidance for attributing and allocating costs to contracts. That guidance may be useful in attributing and allocating costs to segments.

40. SLPSAS 2, *Cash Flow Statements* provides guidance on whether bank overdrafts should be included as a component of cash or should be reported as borrowings.

41. In preparing consolidated financial statements, transactions and balances between controlled entities will be eliminated. However, segment revenue, segment expense, segment assets, and segment liabilities are determined before balances and transactions between entities within the economic entity are eliminated as part of the consolidation process, except to the extent that such intra-economic entity balances and transactions are between entities within a single segment.

42. While the accounting policies used in preparing and presenting the financial statements of the entity as a whole are also the fundamental segment accounting policies, segment accounting policies include, in addition, policies that relate specifically to segment reporting, such as the method of pricing inter-segment transfers, and the basis for allocating revenues and expenses to segments.

Segment Accounting Policies

43. Segment information shall be prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements of the consolidated group or entity.

44. There is a presumption that the accounting policies that the governing body and management of an entity have chosen to use in preparing the consolidated or entity-wide financial statements are those that the governing body and management believe are the most appropriate for external reporting purposes. Since the purpose of segment information is to help users of financial statements better understand and make more informed judgments about the entity as a whole, this Standard requires the use, in preparing segment information, of the accounting policies that the governing body and management have chosen for preparation of the consolidated or entity-wide financial statements. That does not mean, however, that the consolidated or entity accounting policies are to be applied to segments as if the segments were separate reporting entities. A detailed calculation done in applying a particular accounting policy at the entity-wide level may be allocated to segments if there is a reasonable basis for doing so. Employee entitlement calculations, for example, are often done for an entity as a whole, but the entity-wide figures may be allocated to segments based on salary and demographic data for the segments.

45. As noted in paragraph 42, accounting policies that deal with entity-only issues such as inter-segment pricing may need to be developed. SLPSAS 1 requires disclosure of accounting policies necessary to understand the financial statements. Consistent with those requirements, segment-specific policies may need to be disclosed.

46. This Standard permits the disclosure of additional segment information that is prepared on a basis other than the accounting policies adopted for the consolidated or entity financial statements provided that:

(a) The information is relevant for performance assessment and decision making purposes; and

(b) The basis of measurement for this additional information is clearly described.

Joint Assets

47. Assets that are jointly used by two or more segments shall be allocated to segments if, and only if, their related revenues and expenses are also allocated to those segments.

48. The way in which asset, liability, revenue, and expense items are allocated to segments depends on such factors as the nature of those items, the activities conducted by the segment, and the relative autonomy of that segment. It is not possible or appropriate to specify a single basis of allocation that should be adopted by all entities. Nor is it appropriate to force allocation of entity asset, liability, revenue, and expense items that relate jointly to two or more segments, if the only basis for making those allocations is arbitrary or difficult to understand. At the same time,

the definitions of segment revenue, segment expense, segment assets, and segment liabilities are interrelated, and the resulting allocations should be consistent. Therefore, jointly used assets are allocated to segments if, and only if, their related revenues and expenses are also allocated to those segments. For example, an asset is included in segment assets if, and only if, the related depreciation or amortization is included in measuring segment expense.

Newly Identified Segments

49. If a segment is identified as a segment for the first time in the current period, prior period segment data that is presented for comparative purposes shall be restated to reflect the newly reported segment as a separate segment, unless it is impracticable to do so.

50. New segments may be reported in financial statements in differing circumstances. For example, an entity may change its internal reporting structure from a service segment structure to a geographical segment structure, and management may consider it appropriate that this segment structure also be adopted for external reporting purposes. An entity may also undertake significant new or additional activities, or increase the extent to which an activity previously operating as an internal support service provides services to external parties. In these cases, new segments may be reported for the first time in the general purpose financial statements. Where this occurs, this Standard requires that prior period comparative data should be restated to reflect the current segment structure where practicable.

Disclosure

51. **The disclosure requirements in paragraphs 52–75 shall be applied to each segment.**

52. **An entity shall disclose segment revenue and segment expense for each segment. Segment revenue from budget appropriation or similar allocation, segment revenue from other external sources, and segment revenue from transactions with other segments shall be separately reported.**

53. **An entity shall disclose the total carrying amount of segment assets for each segment.**

54. **An entity shall disclose the total carrying amount of segment liabilities for each segment.**

55. **An entity shall disclose the total cost incurred during the period to acquire segment assets that are expected to be used during more than one period for each segment.**

56. An entity is encouraged, but not required, to disclose the nature and amount of any items of segment revenue and segment expense that are of

such size, nature, or incidence that their disclosure is relevant to explain the performance of each segment for the period.

57. SLPSAS 1 requires that when items of revenue or expense are material, their nature and amount of such items are disclosed separately. SLPSAS 1 identifies a number of examples of such items, including write-downs of inventories and property, plant, and equipment; provisions for restructurings; disposals of property, plant, and equipment; privatizations and other disposals of long-term investments; discontinued operations; litigation settlements; and reversals of provisions. The encouragement in paragraph 56 is not intended to change the classification of any such items or to change the measurement of such items. The disclosure encouraged by that paragraph, however, does change the level at which the significance of such items is evaluated for disclosure purposes from the entity level to the segment level.

58. This Standard does not require a segment result to be disclosed. However, if a segment result is calculated and disclosed, it is an operating result that does not include finance charges.

59. An entity is encouraged but not required to disclose segment cash flows consistent with the requirements of SLPSAS 2. SLPSAS 2 requires that an entity present a cash flow statement that separately reports cash flows from operating, investing, and financing activities. It also requires the disclosure of information about certain cash flows. The disclosure of cash flow information about each segment can be useful in understanding the entity's overall financial position, liquidity, and cash flows.

60. An entity that does not disclose segment cash flows in accordance with SLPSAS 2 is encouraged, but not required, to disclose for each reportable segment:

(a) Segment expense for depreciation and amortization of segment assets;

(b) Other significant non-cash expenses; and

(c) Significant non-cash revenues that are included in segment revenue.

This will enable users to determine the major sources and uses of cash in respect of segment activities for the period.

61. **An entity shall disclose for each segment the aggregate of the entity's share of the net surplus (deficit) of associates, joint ventures, or other investments accounted for under the equity method, if substantially all of those associates' operations are within that single segment.**

62. While a single aggregate amount is disclosed pursuant to the requirements of paragraph 61, each associate, joint venture, or other equity method

investment is assessed individually to determine whether its operations are substantially all within a segment.

63. **If an entity's aggregate share of the net surplus (deficit) of associates, joint venture, or other investments accounted for under the equity method is disclosed by segment, the aggregate investments in those associates and joint ventures shall also be disclosed by segment.**

64. **An entity shall present a reconciliation between the information disclosed for segments and the aggregated information in the consolidated or entity financial statements. In presenting the reconciliation, segment revenue shall be reconciled to entity revenue from external sources (including disclosure of the amount of entity revenue from external sources not included in any segment's revenue); segment expense shall be reconciled to a comparable measure of entity expense; segment assets shall be reconciled to entity assets; and segment liabilities shall be reconciled to entity liabilities.**

Additional Segment Information

65. As noted previously, it is anticipated that segments will usually be based on the major goods and services the entity provides, the programs it operates, or the activities it undertakes. This is because information about these segments provides users with relevant information about the performance of the entity in achieving its objectives, and enables the entity to discharge its accountability obligations. However, in some organizations, a geographical or other basis may better reflect the basis on which services are provided and resources allocated within the entity and, therefore, will be adopted for the financial statements.

66. This Standard adopts the view that disclosure of minimum information about both service segments and geographical segments is likely to be useful to users for accountability and decision-making purposes. Therefore, if an entity reports segment information on the basis of:

(a) The major goods and services the entity provides, the programs it operates, the activities it undertakes, or other service segments, it is also encouraged to report the following for each geographical segment that is reported internally to the governing body and the senior manager of the entity:

(i) Segment expense;

(ii) Total carrying amount of segment assets; and

(iii) Total outlay during the period to acquire segment assets that are expected to be used during more than one period (property, plant, equipment, and intangible assets); and

(b) Geographical segments or another basis not encompassed by (a), The entity is encouraged to also report the following segment information for each major service segment that is reported internally to the governing body and the senior manager of the entity:

(i) Segment expense;

(ii) Total carrying amount of segment assets; and

(iii) Total outlay during the period to acquire segment assets that are expected to be used during more than one period (property, plant, equipment, and intangible assets).

Other Disclosure Matters

67. **In measuring and reporting segment revenue from transactions with other segments, inter-segment transfers shall be measured on the basis that they occur. The basis of pricing inter-segment transfers and any change therein shall be disclosed in the financial statements.**

68. **Changes in accounting policies adopted for segment reporting that have a material effect on segment information shall be disclosed, and prior period segment information presented for comparative purposes shall be restated, unless it is impracticable to do so. Such disclosure shall include a description of the nature of the change, the reasons for the change, the fact that comparative information has been restated or that it is impracticable to do so, and the financial effect of the change if it is reasonably determinable. If an entity changes the identification of its segments and it does not restate prior period segment information on the new basis because it is impracticable to do so, then for the purpose of comparison, an entity shall report segment data for both the old and the new bases of segmentation in the year in which it changes the identification of its segments.**

69. Changes in accounting policies adopted by the entity are dealt with in SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors. SLPSAS 3 requires that changes in accounting policy be made only (a) if required by an IPSAS, or (b) if the change will result in reliable and more relevant information about transactions, other events, and conditions in the financial statements of the entity.

70. Changes in accounting policies applied at the entity level that affect segment information are dealt with in accordance with SLPSAS 3. Unless a new IPSAS specifies otherwise, SLPSAS 3 requires that:

(a) A change in accounting policy be applied retrospectively, and that prior period information be restated unless it is impracticable to determine either the cumulative effect or the period-specific effects of the change;

(b) If retrospective application is not practicable for all periods presented, the new accounting policy shall be applied retrospectively from the earliest practicable date; and

(c) If it is impracticable to determine the cumulative effect of applying the new accounting policy at the start of the current period, the policy shall be applied prospectively from the earliest date practicable.

71. Some changes in accounting policies relate specifically to segment reporting. Examples include changes in identification of segments and changes in the basis for allocating revenues and expenses to segments. Such changes can have a significant impact on the segment information reported, but will not change aggregate financial information reported for the entity. To enable users to understand the changes and to assess trends, prior period segment information that is included in the financial statements for comparative purposes is restated, if practicable, to reflect the new accounting policy.

72. Paragraph 67 requires that, for segment reporting purposes, inter-segment transfers should be measured on the basis that the entity actually used to price those transfers. If an entity changes the method that it actually uses to price inter-segment transfers, that is not a change in accounting policy for which prior period segment data should be restated pursuant to paragraph 68. However, paragraph 67 requires disclosure of the change.

73. If not otherwise disclosed in the financial statements or elsewhere in the annual report, an entity shall indicate:

(a) The types of goods and services included in each reported service segment;

(b) The composition of each reported geographical segment; and

(c) If neither a service nor geographical basis of segmentation is adopted, the nature of the segment and activities encompassed by it.

Segment Operating Objectives

74. If not otherwise disclosed in the financial statements or elsewhere in the annual report, the entity is encouraged to disclose the broad operating objectives established for each segment at the commencement of the reporting period, and to comment on the extent to which those objectives were achieved.

75. To enable users to assess the performance of an entity in achieving its service delivery objectives, it is necessary to communicate those objectives to users. The disclosure of information about the composition of each segment, the service delivery objectives of those segments, and the extent

to which those objectives were achieved will support this assessment. This information will also enable the entity to better discharge its accountability obligations. In many cases, this information will be included in the annual report as part of the report of the governing body or the senior manager. In such cases, disclosure of this information in the financial statements is not necessary.

Effective Date

76. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1, 2018. Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1, 2018, it shall disclose that fact.**

77. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Implementation Guidance

This guidance accompanies, but is not part of, SLPSAS 17.

Summary of Required Disclosures

[¶xx] refers to paragraph xx in the Standard.

Disclosures

Total expense by segment [¶52]

Total revenue by segment [¶52]

Revenue from budget appropriation or similar allocation by segment [¶52]

Revenue from external sources (other than appropriation or similar allocation) by segment [¶52]

Revenue from transactions with other segments by segment [¶52]

Carrying amount of segment assets by segment [¶53]

Segment liabilities by segment [¶54]

Cost to acquire assets by segment [¶55]

Share of net surplus (deficit) of [¶61] and investment in [¶63] equity method associates or joint ventures by segment (if substantially all within a single segment)

Reconciliation of revenue, expense, assets and liabilities by segment [¶64]

Other Disclosures

Basis of pricing inter-segment transfers and any changes therein [¶67]

Changes in segment accounting policies [¶68]

Types of products and services in each service segment [¶73]

Composition of each geographical segment [¶73]

If neither a service nor geographical basis of segmentation is adopted, the nature of the segments and activities encompassed by each segment [¶73]

Qualitative Characteristics of Financial Reporting

IG1. Paragraph 15 of this Standard requires the development of accounting policies to ensure that the financial statements provide information that meets a number of qualitative characteristics. This guidance summarizes the qualitative characteristics of financial reporting.

IG2. Qualitative characteristics are the attributes that make the information provided in financial statements useful to users. The four principal qualitative characteristics are understandability, relevance, reliability and comparability.

Understandability

IG3. Information is understandable when users might reasonably be expected to comprehend its meaning. For this purpose, users are assumed to have a reasonable knowledge of the entity's activities and the environment in which it operates, and to be willing to study the information.

IG4. Information about complex matters should not be excluded from the financial statements merely on the grounds that it may be too difficult for certain users to understand.

Relevance

IG5. Information is relevant to users if it can be used to assist in evaluating past, present, or future events or in confirming or correcting past evaluations. In order to be relevant, information must also be timely.

Materiality

IG6. The relevance of information is affected by its nature and materiality.

IG7. Information is material if its omission or misstatement could influence the decisions of users or assessments made on the basis of the financial statements. Materiality depends on the nature or size of the item or error judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point, rather than being a primary qualitative characteristic that information must have if it is to be useful.

Reliability

IG8. Reliable information is free from material error and bias, and can be depended on by users to represent faithfully that which it purports to represent or could reasonably be expected to represent.

Faithful Representation

IG9. For information to represent faithfully transactions and other events, it should be presented in accordance with the substance of the transactions and other events, and not merely their legal form.

Substance Over Form

IG10. If information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance and economic reality, and not merely their legal form. The substance of transactions or other events is not always consistent with their legal form.

Neutrality

IG11. Information is neutral if it is free from bias. Financial statements are not neutral if the information they contain has been selected or presented in a manner designed to influence the making of a decision or judgment in order to achieve a predetermined result or outcome.

Prudence

IG12. Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or revenue are not overstated, and liabilities or expenses are not understated.

IG13. However, the exercise of prudence does not allow, for example, the creation of hidden reserves or excessive provisions, the deliberate understatement of assets or revenue, or the deliberate overstatement of liabilities or expenses, because the financial statements would not be neutral and, therefore, not have the quality of reliability.

Completeness

IG14. The information in financial statements should be complete within the bounds of materiality and cost.

Comparability

IG15. Information in financial statements is comparable when users are able to identify similarities and differences between that information and information in other reports.

IG16. Comparability applies to the:

(a) comparison of financial statements of different entities; and

(b) comparison of the financial statements of the same entity over periods of time.

IG17. An important implication of the characteristic of comparability is that users need to be informed of the policies employed in the preparation of financial statements, changes to those policies, and the effects of those changes.

IG18. Because users wish to compare the performance of an entity over time, it is important that financial statements show corresponding information for preceding periods.

Constraints on Relevant and Reliable Information

Timeliness

IG19. If there is an undue delay in the reporting of information, it may lose its relevance. To provide information on a timely basis, it may often be necessary to report before all aspects of a transaction are known, thus impairing reliability. Conversely, if reporting is delayed until all aspects are known, the information may be highly reliable but of little use to users who have had to make decisions in the interim. In achieving a balance between relevance and reliability, the overriding consideration is how best to satisfy the decision making needs of users.

Balance between Benefit and Cost

IG20. The balance between benefit and cost is a pervasive constraint. The benefits derived from information should exceed the cost of providing it. The evaluation of benefits and costs is, however, substantially a matter of judgment. Furthermore, the costs do not always fall on those users who enjoy the benefits. Benefits may also be enjoyed by users other than those for whom the information was prepared. For these reasons, it is difficult to apply a benefit-cost test in any particular case. Nevertheless, standard setters, as well as those responsible for the preparation of financial statements and users of financial statements, should be aware of this constraint.

Balance between Qualitative Characteristics

IG21. In practice a balancing, or trade-off, between qualitative characteristics is often necessary. Generally the aim is to achieve an appropriate balance among the characteristics in order to meet the objectives of financial statements. The relative importance of the characteristics in different cases is a matter of professional judgment.

Illustrative Example

This example accompanies, but is not part of, SLPSAS 17.

The schedule and related note presented in this example illustrate the segment disclosures that this Standard would require for an education authority that is predominantly funded by appropriation, but (a) provides some educational services on a commercial basis to the employees of major corporations, and (b) has joined with a commercial venture to establish a private education foundation that operates on a commercial basis. The Authority has significant influence over, but does not control, that foundation. For illustrative purposes, the example presents comparative data for two years. Segment data is required for each year for which a complete set of financial statements is presented

Schedule A - Information about Segments (in millions of rupees)

	Primary/ Secondary		Tertiary		Special Services		Other Services		Eliminations		Consolidated	
	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1
SEGMENT REVENUE												
Appropriation	48	40	22	23	10	10	7	7				
Fees from external sources	5	4	—	—	9	6	—	—				
Inter-segment transfers	10	6	6	7	2	4	2	2				
Total Segment Revenue	63	50	28	30	21	20	9	9	20	19	101	90
SEGMENT REVENUE												
Total Segment Revenue	(39)	(31)	(13)	(13)	(13)	(13)	(2)	(2)				
Depreciation	(9)	(7)	(5)	(7)	(5)	(3)	(1)	(1)				
Other expenses	(12)	(11)	(10)	(9)	(5)	(5)	(2)	(2)				
Total Segment Expenses	(60)	(49)	(28)	(29)	(23)	(21)	(5)	(5)	20	19	(96)	(85)

	Primary/ Secondary		Tertiary		Special Services		Other Services		Eliminations		Consolidated	
	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1
Unallocated central expenses											(7)	(9)
Deficit from Operating Activities											(2)	(4)
Interest expense											(4)	(3)
Interest revenue											2	3
Share of net surpluses of associates							8	7			8	7
Surplus for the period											4	3

	Primary/ Secondary		Tertiary		Special Services		Other Services		Eliminations		Consolidated	
	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1
OTHER INFORMATION												
Segment assets	54	50	34	30	10	10	10	9			108	99
Investment in associates (equity method)							32	26			32	26
Unallocated central assets											35	30
Consolidated Total Assets											175	155
Segment liabilities	25	15	8	11	8	8	1	1			42	35
Unallocated corporate liabilities											40	55
Consolidated Total Liabilities											82	90
Capital expenditure	13	10	9	5	4	0	2	3				
Non-cash expense excluding depreciation	(8)	(2)	(3)	(3)	(2)	(2)	(1)	(1)				
Non-cash revenue	—	—	—	—	1	1	—	—				

The Authority is organized and reports to the governing body on the basis of four major functional areas: primary and secondary education; tertiary education; special education services; and other services, each headed by a director. Operations of the special education services segment includes provision of educational services on a commercial basis to the employees of major corporations. In providing these services to external parties, the commercial services unit of the segment uses, on a fee for service basis, services provided by the primary/secondary and tertiary segments. These inter-segment transfers are eliminated on consolidation. Information reported about these segments is used by the governing board and senior management as a basis for evaluating the entity's past performance in achieving its objectives and for making decisions about the future allocation of resources. The disclosure of information about these segments is also considered appropriate for external reporting purposes.

The majority of the Authority's operations are domestic, except that as part of an aid program it has established facilities in Eastern Europe for the provision of secondary educational services. Total cost of services provided in Eastern Europe is 5 million (4 million in 20X1). Total carrying amount of the educational facilities in Eastern Europe are 3 million (6.5 million in 20X1). There were no outlays on the acquisition of capital assets in Eastern Europe during 20X2 or 20X1.

Inter-segment transfers: segment revenue and segment expense include revenue and expense arising from transfers between segments. Such transfers are usually accounted for at cost and are eliminated on consolidation. The amount of these transfers was 20 million (19 million in 19X1).

Investments in associates are accounted for using the equity method. The Authority owns 40% of the capital stock of EuroED Ltd, a specialist education foundation providing educational services internationally on a commercial basis under contract to multilateral lending agencies. The investment is accounted for by the equity method. The investment in, and the Authority's share of, EuroED's net profit are excluded from segment assets and segment revenue.

However they are shown separately under the other services segment, which is responsible for the administration of the investment in the associate.

A full report of the objectives established for each segment and the extent to which those objectives have been achieved is included in the Review of Operations, included elsewhere in this report.

SLPSAS – 18 – Agriculture

Acknowledgement

Agriculture (SLPSAS – 18) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

CONTENTS

Sri Lanka Public Sector Accounting Standard 18, Agriculture is set out in paragraphs 1–57. All the paragraphs have equal authority. SLPSAS 18 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe the accounting treatment and disclosures for agricultural activity.

Scope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard for the following when they relate to agricultural activity:**

   (a) Biological assets; and

   (b) Agricultural produce at the point of harvest.

3. This Standard does not apply to:

   (a) Land related to agricultural activity (see SLPSAS 13, Investment Property and SLPSAS 7, Property, Plant, and Equipment);

   (b) Intangible assets related to agricultural activity (see SLPSAS 20, Intangible Assets); and

   (c) Biological assets held for the provision or supply of services.

4. Biological assets are used in many activities undertaken by public sector entities. When biological assets are used for research, education, transportation, entertainment, recreation, customs control or in any other activities that are not agricultural activities as defined in paragraph 9 of this Standard, those biological assets are not accounted for in accordance with this Standard. Where those biological assets meet the definition of an asset, other SLPSASs should be considered in determining the appropriate accounting (e.g., SLPSAS 9, Inventories and SLPSAS 7).

5. This Standard is applied to agricultural produce, which is the harvested product of the entity's biological assets, only at the point of harvest. Thereafter, SLPSAS 9, or another applicable Standard, is applied. Accordingly, this Standard does not deal with the processing of agricultural produce after harvest; for example, the processing of grapes into wine by a vintner who has grown the grapes. While such processing may be a logical and natural extension of agricultural activity, and the events taking place may bear some similarity to biological transformation, such processing is not included within the definition of agricultural activity in this Standard.

6. The table below provides examples of biological assets, agricultural produce, and products that are the result of processing after harvest:

Biological assets	**Agricultural produce**	**Products that are the result of processing after harvest**
Sheep	Wool	Yarn, carpet
Trees in a plantation forest	Felled trees	Logs, lumber
Plants	Cotton	Thread, clothing
	Harvested cane	Sugar
Dairy cattle	Milk	Cheese
Pigs	Carcass	Sausages, cured hams
Bushes	Leaf	Tea, cured tobacco
Vines	Grapes	Wine
Fruit trees	Picked fruit	Processed fruit

7. **This Standard applies to all public sector entities other than Government Business Enterprises**.

8. *The Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

Definitions

Agriculture-related Definitions

9. **The following terms are used in this Standard with the meanings specified:**

Agricultural activity is the management by an entity of the biological transformation and harvest of biological assets for:

- **Sale;**
- **Distribution at no charge or for a nominal charge; or**
- **Conversion into agricultural produce or into additional biological assets for sale or for distribution at no charge or for a nominal charge.**

Agricultural produce is the harvested product of the entity's biological assets.

A biological asset is a living animal or plant.

Biological transformation comprises the processes of growth, degeneration, production, and procreation that cause qualitative or quantitative changes in a biological asset.

Costs to sell are the incremental costs directly attributable to the disposal of an asset, excluding finance costs and income taxes. Disposal may occur through sale or through distribution at no charge or for a nominal charge.

A group of biological assets is an aggregation of similar living animals or plants.

Harvest is the detachment of produce from a biological asset or the cessation of a biological asset's life processes.

10. Agricultural activity covers a diverse range of activities; for example, raising livestock, forestry, annual or perennial cropping, cultivating orchards and plantations, floriculture, and aquaculture (including fish farming). Certain common features exist within this diversity:

(a) *Capability to change.* Living animals and plants are capable of biological transformation;

(b) *Management of change*. Management facilitates biological transformation by enhancing, or at least stabilizing, conditions necessary for the process to take place (for example, nutrient levels, moisture, temperature, fertility, and light). Such management distinguishes agricultural activity from other activities. For example, harvesting from unmanaged sources (such as ocean fishing and deforestation) is not agricultural activity; and

(c) *Measurement of change.* The change in quality (for example, genetic merit, density, ripeness, fat cover, protein content, and fiber strength) or quantity (for example, progeny, weight, cubic meters, fiber length or diameter, and number of buds) brought about by biological transformation or harvest is measured and monitored as a routine management function.

11. Biological transformation results in the following types of outcomes:

(a) Asset changes through (i) growth (an increase in quantity or improvement in quality of an animal or plant), (ii) degeneration (a decrease in the quantity or deterioration in quality of an animal or plant), or (iii) procreation (creation of additional living animals or plants); or

(b) Production of agricultural produce such as latex, tea leaf, wool, and milk.

General Definitions

12. **Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the** *Glossary of Defined Terms published separately*.

Recognition and Measurement

13. An entity shall recognize a biological asset or agricultural produce when and only when:

- **(a) The entity controls the asset as a result of past events;**
- **(b) It is probable that future economic benefits or service potential associated with the asset will flow to the entity; and**
- **(c) The fair value or cost of the asset can be measured reliably.**

14. The fair value of an asset is based on its present location and condition. As a result, for example, the fair value of cattle at a farm is the price for the cattle in the relevant market less the transport and other costs of getting the cattle either to that market or to the location where it will be distributed at no charge or for a nominal charge.

15. In agricultural activity, control may be evidenced by, for example, legal ownership of cattle and the branding or otherwise marking of the cattle on acquisition, birth, or weaning. The future benefits or service potential are normally assessed by measuring the significant physical attributes.

16. **A biological asset shall be measured on initial recognition and at each reporting date at its fair value less costs to sell, except for the case described in paragraph 34 where the fair value cannot be measured reliably.**

17. Where an entity acquires a biological asset through a non-exchange transaction, the biological asset is measured on initial recognition and at each reporting date in accordance with paragraph 16.

18. Agricultural produce harvested from an entity's biological assets shall be measured at its fair value less costs to sell at the point of harvest. Such measurement is the cost at that date when applying SLPSAS 9, or another applicable Standard.

19. The determination of fair value for a biological asset or agricultural produce may be facilitated by grouping biological assets or agricultural produce according to significant attributes; for example, by age or quality. An entity selects the attributes corresponding to the attributes used in the market as a basis for pricing.

20. Entities often enter into contracts to sell their biological assets or agricultural produce at a future date. Contract prices are not necessarily relevant in determining fair value, because fair value reflects the current market in which a willing buyer and seller would enter into a transaction. As a result,

the fair value of a biological asset or agricultural produce is not adjusted because of the existence of a contract. In some cases, a contract for the sale of a biological asset or agricultural produce in an exchange transaction may be an onerous contract, as defined in SLPSAS 8, Provisions, Contingent Liabilities and Contingent Assets. SLPSAS 8 applies to onerous contracts.

21. If an active market exists for a biological asset or agricultural produce in its present location and condition, the quoted price in that market is the appropriate basis for determining the fair value of that asset. If an entity has access to different active markets, the entity uses the most relevant one. For example, if an entity has access to two active markets, it would use the price existing in the market expected to be used.

22. If an active market does not exist, an entity uses one or more of the following, when available, in determining fair value:

    (a) The most recent market transaction price, provided that there has not been a significant change in economic circumstances between the date of that transaction and the reporting date;

    (b) Market prices for similar assets with adjustment to reflect differences; and

    (c) Sector benchmarks such as the value of an orchard expressed per export tray, bushel, or hectare, and the value of cattle expressed per kilogram of meat.

23. In some cases, the information sources listed in paragraph 22 may suggest different conclusions as to the fair value of a biological asset or agricultural produce. An entity considers the reasons for those differences, in order to arrive at the most reliable estimate of fair value within a relatively narrow range of reasonable estimates.

24. In some circumstances, market-determined prices or values may not be available for a biological asset in its present condition. In these circumstances, an entity uses the present value of expected net cash flows from the asset discounted at a current market-determined rate in determining fair value.

25. The objective of a calculation of the present value of expected net cash flows is to determine the fair value of a biological asset in its present location and condition. An entity considers this in determining an appropriate discount rate to be used and in estimating expected net cash flows. In determining the present value of expected net cash flows, an entity includes the net cash flows that market participants would expect the asset to generate in its most relevant market.

26. An entity does not include any cash flows for financing the assets, taxation, or re establishing biological assets after harvest (for example, the cost of replanting trees in a plantation forest after harvest).

27. In agreeing an arm's length transaction price, knowledgeable, willing buyers and sellers consider the possibility of variations in cash flows. It follows that fair value reflects the possibility of such variations. Accordingly, an entity incorporates expectations about possible variations in cash flows into either the expected cash flows, or the discount rate, or some combination of the two. In determining a discount rate, an entity uses assumptions consistent with those used in estimating the expected cash flows, to avoid the effect of some assumptions being double-counted or ignored.

28. Cost may sometimes approximate fair value, particularly when:

    (a) Little biological transformation has taken place since initial cost incurrence (for example, for fruit tree seedlings planted immediately prior to reporting date); or

    (b) The impact of the biological transformation on price is not expected to be material (for example, for the initial growth in a 30 year pine plantation production cycle).

29. Biological assets are often physically attached to land (for example, trees in a plantation forest). There may be no separate market for biological assets that are attached to the land but an active market may exist for the combined assets, that is, for the biological assets, raw land, and land improvements, as a package. An entity may use information regarding the combined assets to determine fair value for the biological assets. For example, the fair value of raw land and land improvements may be deducted from the fair value of the combined assets to arrive at the fair value of biological assets.

Gains and Losses

30. **A gain or loss arising on initial recognition of a biological asset at fair value less costs to sell and from a change in fair value less costs to sell of a biological asset shall be included in surplus or deficit for the period in which it arises**.

31. A loss may arise on initial recognition of a biological asset, because costs to sell are deducted in determining fair value less costs to sell of a biological asset. A gain may arise on initial recognition of a biological asset, such as when a calf is born.

32. **A gain or loss arising on initial recognition of agricultural produce at fair value less costs to sell shall be included in surplus or deficit for the period in which it arises.**

33. A gain or loss may arise on initial recognition of agricultural produce as a result of harvesting.

Inability to Measure Fair Value Reliably

34. **There is a presumption that fair value can be measured reliably for a biological asset. However, that presumption can be rebutted only on initial recognition for a biological asset for which market-determined prices or values are not available, and for which alternative estimates of fair value are determined to be clearly unreliable. In such a case, that biological asset shall be measured at its cost less any accumulated depreciation and any accumulated impairment losses. Once the fair value of such a biological asset becomes reliably measurable, an entity shall measure it at its fair value less costs to sell. Once a non current biological asset meets the criteria to be classified as held for sale (or is included in a disposal group that is classified as held for sale) in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations, it is presumed that fair value can be measured reliably.**

35. The presumption in paragraph 34 can be rebutted only on initial recognition. An entity that has previously measured a biological asset at its fair value less costs to sell continues to measure the biological asset at its fair value less costs to sell until disposal.

36. In all cases, an entity measures agricultural produce at the point of harvest at its fair value less costs to sell. This Standard reflects the view that the fair value of agricultural produce at the point of harvest can always be measured reliably.

37. In determining cost, accumulated depreciation and accumulated impairment losses, an entity considers SLPSAS 9 and SLPSAS 7.

Disclosure

General

38. **An entity shall disclose the aggregate gain or loss arising during the current period on initial recognition of biological assets and agricultural produce and from the change in fair value less costs to sell of biological assets.**

39. An entity shall provide a description of biological assets that distinguishes between consumable and bearer biological assets and between biological assets held for sale and those held for distribution at no charge or for a nominal charge.

40. Consumable biological assets are those that are held for harvest as agricultural produce or for sale or distribution at no charge or for a nominal charge as biological assets. Examples of consumable biological assets are animals and plants for one-time use, such as livestock intended for the production of meat, livestock held for sale, fish in farms, crops such as maize and wheat, and trees being grown for lumber. Bearer biological assets are those biological assets that are used repeatedly or continuously for more than one year in an agricultural activity. Bearer biological assets

are not agricultural produce but, rather, are self-regenerating. Examples of types of animals that are bearer biological assets include breeding stocks (including fish and poultry), livestock from which milk is produced, and sheep or other animals used for wool production. Examples of types of plants that are bearer biological assets include trees, vines and shrubs cultivated for fruits, nuts, sap, resin, bark and leaf products and trees from which firewood is harvested while the tree remains.

41. The disclosures required by paragraph 39 would take the form of a quantified description. The quantified description may be accompanied by a narrative description.

42. In making the disclosures required by paragraph 39, an entity is also encouraged to distinguish between mature and immature biological assets, as appropriate. These distinctions provide information that may be helpful in assessing the timing of future cash flows and service potential. An entity discloses the basis for making any such distinctions.

43. Mature biological assets are those that have attained harvestable specifications (for consumable biological assets) or are able to sustain regular harvests (for bearer biological assets).

44. **If not disclosed elsewhere in information published with the financial statements, an entity shall describe:**

   (a) The nature of its activities involving each group of biological assets; and

   (b) Non financial measures or estimates of the physical quantities of:

      (i) Each group of the entity's biological assets at the end of the period; and

      (ii) Output of agricultural produce during the period.

45. An entity shall disclose the methods and significant assumptions applied in determining the fair value of each group of agricultural produce at the point of harvest and each group of biological assets.

46. An entity shall disclose the fair value less costs to sell of agricultural produce harvested during the period, determined at the point of harvest.

47. An entity shall disclose:

   (a) The existence and carrying amounts of biological assets whose title is restricted, and the carrying amounts of biological assets pledged as security for liabilities;

   (b) The nature and extent of restrictions on the entity's use or capacity to sell biological assets;

   (c) The amount of commitments for the development or acquisition of biological assets; and

(d) Financial risk management strategies related to agricultural activity.

48. An entity shall present a reconciliation of changes in the carrying amount of biological assets between the beginning and the end of the current period. The reconciliation shall include:

(a) The gain or loss arising from changes in fair value less costs to sell, disclosed separately for bearer biological assets and consumable biological assets;

(b) Increases due to purchases;

(c) Increases due to assets acquired through a non-exchange transaction;

(d) Decreases attributable to sales and biological assets classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations;

(e) Decreases due to distributions at no charge or for a nominal charge;

(f) Decreases due to harvest;

(g) Increases resulting from entity combinations;

(h) Net exchange differences arising on the translation of financial statements into a different presentation currency, and on the translation of a foreign operation into the presentation currency of the reporting entity; and

(i) Other changes.

49. The fair value less costs to sell of a biological asset can change due to both physical changes and price changes in the market. Separate disclosure of physical and price changes is useful in appraising current period performance and future prospects, particularly when there is a production cycle of more than one year. In such cases, an entity is encouraged to disclose, by group or otherwise, the amount of change in fair value less costs to sell included in surplus or deficit due to physical changes and due to price changes. This information is generally less useful when the production cycle is less than one year (for example, when raising chickens or growing cereal crops).

50. Biological transformation results in a number of types of physical change—growth, degeneration, production, and procreation, each of which is observable and measurable. Each of those physical changes has a direct relationship to future economic benefits or service potential. A change in fair value of a biological asset due to harvesting is also a physical change.

51. Agricultural activity is often exposed to climatic, disease and other natural risks. If an event occurs that gives rise to a material item of revenue or expense, the nature and amount of that item are disclosed in accordance with SLPSAS 1. Examples of such an event include an outbreak of a virulent disease, a flood, a severe drought or frost, and a plague of insects.

Additional Disclosures for Biological Assets Where Fair Value Cannot Be Measured Reliably

52. If an entity measures biological assets at their cost less any accumulated depreciation and any accumulated impairment losses (see paragraph 34) at the end of the period, the entity shall disclose for such biological assets:

- **(a) A description of the biological assets;**
- **(b) An explanation of why fair value cannot be measured reliably;**
- **(c) If possible, the range of estimates within which fair value is highly likely to lie;**
- **(d) The depreciation method used;**
- **(e) The useful lives or the depreciation rates used; and**
- **(f) The gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period.**

53. If, during the current period, an entity measures biological assets at their cost less any accumulated depreciation and any accumulated impairment losses (see paragraph 34), an entity shall disclose any gain or loss recognized on disposal of such biological assets and the reconciliation required by paragraph 48 shall disclose amounts related to such biological assets separately. In addition, the reconciliation shall include the following amounts included in surplus or deficit related to those biological assets:

- **(a) Impairment losses;**
- **(b) Reversals of impairment losses; and**
- **(c) Depreciation.**

54. If the fair value of biological assets previously measured at their cost less any accumulated depreciation and any accumulated impairment losses becomes reliably measurable during the current period, an entity shall disclose for those biological assets:

- **(a) A description of the biological assets;**
- **(b) An explanation of why fair value has become reliably measurable; and**

(c) The effect of the change.

Transitional Provision

Initial Adoption of Accrual Accounting

55. **Where an entity initially recognizes biological assets or agricultural produce on the first-time adoption of the accrual basis of accounting, the entity shall report the effect of the initial recognition of those assets, and that produce as an adjustment to the opening balance of accumulated surpluses or deficits for the period in which this Standard is first adopted.**

Effective Date

56. An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1, 2018. Earlier application is encouraged. If an entity applies this Standard for a period beginning before January 1, 2018, it shall disclose that fact.

57. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Illustrative Examples

These examples accompany, but are not part of, SLPSAS 18.

Extracts from statements of financial performance and statements of financial position are provided to show the effects of the transactions described below. These extracts do not necessarily conform to all the disclosure and presentation requirements of other Standards.

The first example illustrates how the disclosure requirements of this Standard might be put into practice for a dairy farming entity. This Standard encourages the separation of the change in fair value less costs to sell of an entity's biological assets into physical change and price change. That separation is reflected in the first example. The second example illustrates how to separate physical change and price change.

Disclosure Requirements

Statement of Financial Position

Entity XYZ	Notes	December 31, 20X8	December 31, 20X17
ASSETS		Rs.	Rs.
Current assets			
Cash		10,000	10,000
Receivables		88,000	65,000
Inventories		82,950	70,650
Total current assets		**180,950**	**145,650**
Non-current assets			
Bearer biological assets			
Dairy livestock – immature		52,060	47,730
Dairy livestock – mature1		372,990	411,840
Subtotal – bearer biological assets	3	425,050	459,570
Property, plant and equipment		1,462,650	1,409,800
Total non-current assets		**1,887,700**	**1,869,370**
Total assets		**2,068,650**	**2,015,020**
LIABILITIES			
Current liabilities			
Payables		122,628	150,020
Total current liabilities		**122,628**	**150,020**
NET ASSETS/EQUITY			
Contributed capital		1,000,000	1,000,000
Accumulated surplus		946,022	865,000
Total net assets/equity		**1,946,022**	**1,865,000**
Total net assets/equity and liabilities		**2,068,650**	**2,015,020**

1 An entity is required to provide a description of biological assets that distinguishes between consumable and bearer biological assets and between those held for sale and those held for distribution at no charge or for a nominal charge. Such disclosures would take the form of a quantified description that may be accompanied by a narrative description. An entity is also encouraged, but not required, to distinguish between mature and immature biological assets, as appropriate. An entity discloses the basis for making any such distinctions. This example shows the disclosure of bearer biological assets on the face of the statement of financial position. Information to meet other disclosure requirements is disclosed in the notes to the financial statements, as permitted.

Statement of Financial Performance

Entity XYZ	Notes	Rs. Year ended December 31, 20X8
Fair value of milk produced		518,240
Gains arising from changes in fair value less costs to sell of dairy livestock held for sale	3	39,930
		558,170
Inventories used		(137,523)
Staff costs		(127,283)
Depreciation expense		(15,250)
Other operating expenses		(197,092)
		(477,148)
Surplus for the period		**81,022**

Statement of Changes in Net Assets/Equity

	Year ended December 31, 20X8		
	Rs.	Rs.	Rs.
	Contributed Capital	**Accumulated Surplus**	**Total**
Balance at January 1, 20X8	1,000,000	865,000	1,865,000
Surplus for the period		81,022	81,022
Balance at December 31, 20X8	**1,000,000**	**946,022**	**1,946,022**

Cash Flow Statement

Entity XYZ	**Year ended December 31, 20X8**
	Rs.
Cash flows from operating activities	
Cash receipts from sales of milk	498,027
Cash receipts from sales of livestock	97,913
Cash paid for supplies and to employees	(504,025)
Cash paid for purchases of livestock	(23,815)
Net cash from operating activities	**68,100**
Cash flows from investing activities	
Purchase of property, plant and equipment	(68,100)
Net cash used in investing activities	**(68,100)**
Net increase in cash	**0**
Cash at beginning of the year	**10,000**
Cash at end of the year	**10,000**

Notes

1. Operations and Principal Activities

Entity XYZ ("the Entity") is engaged in milk production. At December 31, 20X8, the Entity held 419 cows able to produce milk (mature bearer assets) and 137 heifers being raised to produce milk in the future (immature bearer assets). The Entity produced 157,584 kg of milk with a fair value less costs to sell of Rs.518,240 (the fair value of this agricultural produce is determined at the time of milking) in the year ended December 31, 20X8. The Entity does not own any consumable biological assets.

2. Accounting Policies

Livestock and Milk

Livestock are measured at their fair value less costs to sell. The fair value of livestock is determined based on market prices of livestock of similar age, breed, and genetic merit. Milk is initially measured at its fair value less costs to sell at the time of milking. The fair value of milk is determined based on market prices in the local area.

This statement of cash flows reports cash flows from operating activities using the direct method. SLPSAS 2, "Cash Flow Statements" requires that an entity reports cash flows from operating activities using either the direct method or the indirect method. SLPSAS 2 encourages use of the direct method.

3. Biological Assets

Reconciliation of Carrying Amounts of Dairy Livestock	20X8 Rs.
Carrying amount at January 1, 20X8	459,570
Increases due to purchases	26,250
Gain arising from changes in fair value less costs to sell attributable to physical changes	15,350
Gain arising from changes in fair value less costs to sell attributable to price changes	24,580
Decreases due to sales	(100,700)
Carrying amount at December 31, 20X8	**425,050**

4. Financial Risk Management Strategies

The Entity is exposed to financial risks arising from changes in milk prices. The Entity does not anticipate that milk prices will decline significantly in the foreseeable future and, therefore, has not entered into derivative or other contracts to manage the risk of a decline in milk prices. The Entity reviews its outlook for milk prices regularly in considering the need for active financial risk management.

Physical Change and Price Change

The following example illustrates how to separate physical change and price change. Separating the change in fair value less costs to sell between the portion attributable to physical changes and the portion attributable to price changes is encouraged but not required by this Standard.

A herd of ten 2 year old animals was held at January 1, 20X8. One animal aged 2.5 years was purchased on July 1, 20X8 for Rs.108, and one animal was born on July 1, 20X8. No animals were sold or disposed of during the period. Per-unit fair values less costs to sell were as follows:

	Rs.	Rs.
2 year old animal at January 1, 20X8	100	
Newborn animal at July 1, 20X8	70	
2.5 year old animal at July 1, 20X8	108	
Newborn animal at December 31, 20X8	72	
0.5 year old animal at December 31, 20X8	80	
2 year old animal at December 31, 20X8	105	
2.5 year old animal at December 31, 20X8	111	
3 year old animal at December 31, 20X8	120	

3 Separating the increase in fair value less costs to sell between the portion attributableto physical changes and the portion attributable to price changes is encouraged but not required by this Standard.

4. See Footnote 3.

Fair value less costs to sell of herd at January 1, 20X8 (10 x 100)		1,000
Purchase on July 1, 20X8 (1 x 108)		108
Increase in fair value less costs to sell due to price change		
10 × (105 – 100)	50	
1 × (111 – 108)	3	
1 × (72 – 70)	2	
		55
Increase in fair value less costs to sell due to physical change:		
10 × (120 – 105)	150	
1 × (120 – 111)	9	
1 × (80 – 72)	8	
1 × 70 70	70	237
Fair value less costs to sell of herd at December 31, 20X8		
11 × 120	1,320	
1 × 80	80	
		1,400

SLPSAS – 19 – Employee Benefits

Acknowledgement

Employee Benefits (SLPSAS – 19) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

CONTENTS

Appendix A: Application Guidance

Illustrative Examples

Sri Lanka Public Sector Accounting Standard 19, Employee Benefits, is set out in paragraphs 1–178. All the paragraphs have equal authority. SLPSAS 19 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe the accounting and disclosure for employee benefits. The Standard requires an entity to recognize:

   (a) A liability when an employee has provided service in exchange for employee benefits to be paid in the future; and

   (b) An expense when the entity consumes the economic benefits or service potential arising from service provided by an employee in exchange for employee benefits.

Scope

2. **This Standard shall be applied by an employer in accounting for all employee benefits, except share-based transactions (see the relevant Sri Lanka Accounting Standard dealing with share-based transactions).**

3. This Standard does not deal with reporting by employee retirement benefit plans (see the relevant Sri Lanka Accounting Standard dealing with employee retirement benefit plans). This Standard does not deal with benefits provided by composite social security programs that are not consideration in exchange for service rendered by employees or past employees of public sector entities.

4. The employee benefits to which this Standard applies include those provided:

   (a) Under formal plans or other formal agreements between an entity and individual employees, groups of employees, or their representatives;

   (b) Under legislative requirements, or through industry arrangements, whereby entities are required to contribute to national, state, industry, or other multi-employer plans, or where entities are required to contribute to the composite social security program; or

   (c) By those informal practices that give rise to a constructive obligation. Informal practices give rise to a constructive obligation where the entity has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the entity's informal practices would cause unacceptable damage to its relationship with employees.

5. Employee benefits include:

   (a) Short-term employee benefits, such as wages, salaries, and social security contributions; paid annual leave and paid sick leave; profit-sharing and bonuses (if payable within twelve months of the end of the period); and non monetary benefits (such as medical care, housing, cars, and free or subsidized goods or services) for current employees;

   (b) Post-employment benefits such as pensions, other retirement benefits, post-employment life insurance, and post-employment medical care;

(c) Other long-term employee benefits, which may include long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are not payable wholly within twelve months after the end of the period, profit-sharing, bonuses, and deferred compensation; and

(d) Termination benefits.

Because each category identified in (a)–(d) above has different characteristics, this Standard establishes separate requirements for each category.

6. Employee benefits include benefits provided to either employees or their dependants, and may be settled by payments (or the provision of goods or services) made either directly to the employees, to their spouses, children, or other dependants, or to others, such as insurance companies.

7. An employee may provide services to an entity on a full-time, part-time, permanent, casual, or temporary basis. For the purpose of this Standard, employees include key management personnel as defined in SLPSAS 14, *Related Party Disclosures*.

8. **This Standard applies to all public sector entities other than Government Business Enterprises.**

9. The *Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply SLFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements*.

Definitions

10. **The following terms are used in this Standard with the meanings specified:**

<u>Actuarial gains and losses comprise:</u>

(a) Experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred); and

(b) The effects of changes in actuarial assumptions.

<u>Assets held by a long-term employee benefit fund</u> are assets (other than non-transferable financial instruments issued by the reporting entity) that:

(a) Are held by an entity (a fund) that is legally separate from the reporting entity and exists solely to pay or fund employee benefits; and

(b) Are available to be used only to pay or fund employee benefits, are not available to the reporting entity's own creditors (even in bankruptcy), and cannot be returned to the reporting entity, unless either:

(i) The remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting entity; or

(ii) The assets are returned to the reporting entity to reimburse it for employee benefits already paid.

Composite social security programs are established by legislation, and

(a) Operate as multi-employer plans to provide post-employment benefits; as well as to

(b) Provide benefits that are not consideration in exchange for service rendered by employees.

Current service cost is the increase in the present value of the defined benefit obligation resulting from employee service in the current period.

Defined benefit plans are post-employment benefit plans other than defined contribution plans.

Defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund), and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees.

Interest cost is the increase during a period in the present value of a defined benefit obligation that arises because the benefits are one period closer to settlement.

Multi-employer plans are defined contribution plans (other than state plans and composite social security programs) or defined benefit plans (other than state plans) that:

(a) Pool the assets contributed by various entities that are not under common control; and

(b) Use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees concerned.

<u>Other long-term employee benefits</u> are employee benefits (other than post-employment benefits and termination benefits) that are not due to be settled within twelve months after the end of the period in which the employees render the related service.

<u>Past service cost</u> is the change in the present value of the defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (when benefits are introduced or changed so that the present value of the defined benefit obligation increases) or negative (when existing benefits are changed so that the present value of the defined benefit obligation decreases).

<u>Plan assets comprise:</u>

(a) **Assets held by a long-term employee benefit fund; and**

(b) **Qualifying insurance policies.**

<u>Post-employment benefits</u> are employee benefits (other than termination benefits) which are payable after the completion of employment.

<u>Post-employment benefit plans</u> are formal or informal arrangements under which an entity provides post-employment benefits for one or more employees.

The <u>present value of a defined benefit obligation</u> is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

<u>A qualifying insurance policy</u> is an insurance policy- issued by an insurer that is not a related party (as defined in SLPSAS 14) of the reporting entity, if the proceeds of the policy:

(a) **Can be used only to pay or fund employee benefits under a defined benefit plan; and**

(b) **Are not available to the reporting entity's own creditors (even in bankruptcy) and cannot be paid to the reporting entity, unless either:**

  (i) **The proceeds represent surplus assets that are not needed for the policy to meet all the related employee benefit obligations; or**

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* A qualifying insurance policy is not necessarily an insurance contract (see the Sri Lanka Accounting Standard dealing with insurance contracts).

(ii) **The proceeds are returned to the reporting entity to reimburse it for employee benefits already paid.**

The return on plan assets is interest, dividends or similar distributions and other revenue derived from the plan assets, together with realized and unrealized gains or losses on the plan assets, less any costs of administering the plan (other than those included in the actuarial assumptions used to measure the defined benefit obligation) and less any tax payable by the plan itself.

Short-term employee benefits are employee benefits (other than termination benefits) that are due to be settled within twelve months after the end of the period in which the employees render the related service.

State plans are plans other than composite social security programs established by legislation that operate as if they are multi-employer plans for all entities in economic categories laid down in legislation.

Termination benefits are employee benefits payable as a result of either:

(a) **An entity's decision to terminate an employee's employment before the normal retirement date; or**

(b) **An employee's decision to accept voluntary redundancy in exchange for those benefits.**

Vested employee benefits are employee benefits that are not conditional on future employment.

Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of *Defined Terms* published separately.

Short-Term Employee Benefits

11. Short-term employee benefits include items such as:

(a) Wages, salaries, and social security contributions;

(b) Short-term compensated absences (such as paid annual leave and paid sick leave) where the compensation for the absences is due to be settled within twelve months after the end of the period in which the employees render the related employee service;

(c) Performance related bonuses and profit-sharing payable within twelve months after the end of the period in which the employees render the related service; and

(d) Non monetary benefits (such as medical care, housing, cars, and free or subsidized goods or services) for current employees.

12. Accounting for short-term employee benefits is generally straightforward, because no actuarial assumptions are required to measure the obligation or the cost, and there is no possibility of any actuarial gain or loss. Moreover, short-term employee benefit obligations are measured on an undiscounted basis.

Recognition and Measurement

All Short-Term Employee Benefits

13. **When an employee has rendered service to an entity during an accounting period, the entity shall recognize the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:**

    (a) **As a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an entity shall recognize that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and**

    (b) **As an expense, unless another Standard requires or permits the inclusion of the benefits in the cost of an asset (see, for example, SLPSAS 9, Inventories, and SLPSAS 7, Property, Plant, and Equipment.**

    Paragraphs 14, 17, and 20 explain how an entity shall apply this requirement to short-term employee benefits in the form of compensated absences and bonus and profit-sharing plans.

Short-Term Compensated Absences

14. An entity shall recognize the expected cost of short-term employee benefits in the form of compensated absences under paragraph 13 as follows:

    (a) **In the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and**

    (b) **In the case of non-accumulating compensated absences, when the absences occur.**

15. An entity may compensate employees for absence for various reasons, including vacation, sickness and short-term disability, maternity or paternity, jury service, and military service. Entitlement to compensated absences falls into two categories:

    (a) Accumulating; and

    (b) Non-accumulating.

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

full. Accumulating compensated absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the entity) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving). An obligation arises as employees render service that increases their entitlement to future compensated absences. The obligation exists, and is recognized, even if the compensated absences are non vesting, although the possibility that employees may leave before they use an accumulated non vesting entitlement affects the measurement of that obligation.

17. **An entity shall measure the expected cost of accumulating compensated absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the reporting date**.

18. The method specified in paragraph 17 measures the obligation at the amount of the additional payments that are expected to arise solely from the fact that the benefit accumulates. In many cases, an entity may not need to make detailed computations to estimate that there is no material obligation for unused compensated absences. For example, a sick leave obligation is likely to be material only if there is a formal or informal understanding that unused paid sick leave may be taken as paid vacation.

19. Non-accumulating compensated absences do not carry forward; they lapse if the current period's entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the entity. This is commonly the case for sick pay (to the extent that unused past entitlement does not increase future entitlement), maternity or paternity leave, and compensated absences for jury service or military service. An entity recognizes no liability or expense until the time of the absence, because employee service does not increase the amount of the benefit.

Bonus Payments and Profit-Sharing Payments

20. **An entity shall recognize the expected cost of bonus payments and profit-sharing payments under paragraph 13 when, and only when:**

    (a) **The entity has a present legal or constructive obligation to make such payments as a result of past events; and**

    (b) **A reliable estimate of the obligation can be made.**

    A present obligation exists when, and only when, the entity has no realistic alternative but to make the payments.

21. In the public sector, some entities have bonus plans that are related to service delivery objectives or aspects of financial performance. Under such plans, employees receive specified amounts, dependent on an assessment of their contribution to the achievement of the objectives of the entity or a segment of the entity. In some cases, such plans may be

for groups of employees, such as when performance is evaluated for all or some employees in a particular segment, rather than on an individual basis. Because of the objectives of public sector entities, profit-sharing plans are far less common in the public sector than for profit-oriented entities. However, they are likely to be an aspect of employee remuneration in segments of public sector entities that operate on a commercial basis. Some public sector entities may not operate profit-sharing schemes, but may evaluate performance against financially based measures such as the generation of revenue streams and the achievement of budgetary targets. Some bonus plans may entail payments to all employees who rendered employment services in a reporting period, even though they may have left the entity before the reporting date. However, under other bonus plans, employees receive payments only if they remain with the entity for a specified period, for example, a requirement that employees render services for the whole of the reporting period. Such plans create a constructive obligation as employees render service that increases the amount to be paid if they remain in service until the end of the specified period. The measurement of such constructive obligations reflects the possibility that some employees may leave without receiving profit-sharing payments. Paragraph 23 provides further conditions that are to be satisfied before an entity can recognize the expected cost of performance-related payments, bonus payments, and profit-sharing payments.

22. An entity may have no legal obligation to pay a bonus. Nevertheless, in some cases, an entity has a practice of paying bonuses. In such cases, the entity has a constructive obligation because the entity has no realistic alternative but to pay the bonus. The measurement of the constructive obligation reflects the possibility that some employees may leave without receiving a bonus.

23. An entity can make a reliable estimate of its legal or constructive obligation under a performance-related payment scheme, bonus plan, or profit-sharing scheme when, and only when:

    (a) The formal terms of the plan contain a formula for determining the amount of the benefit;

    (b) The entity determines the amounts to be paid before the financial statements are authorized for issue; or

    (c) Past practice gives clear evidence of the amount of the entity’s constructive obligation.

24. An obligation under bonus plans and profit-sharing plans results from employee service, and is recognized as an expense in surplus or deficit.

25. If bonus payments and profit shares are not due wholly within twelve months after the end of the period in which the employees render the related service, those payments are other long-term employee benefits (see paragraphs 147–153).

Disclosure

26. Although this Standard does not require specific disclosures about short-term employee benefits, other Standards may require disclosures. For example, SLPSAS 14 requires disclosures of the aggregate remuneration of key management personnel and SLPSAS 1 requires the disclosure of information about employee benefits.

Post-employment Benefits-Distinction between Defined Contribution Plans and Defined Benefit Plans

27. Post-employment benefits include, for example:

    (a) Retirement benefits, such as pensions; and

    (b) Other post-employment benefits, such as post-employment life insurance, and post-employment medical care.

    Arrangements whereby an entity provides post-employment benefits are post-employment benefit plans. An entity applies this Standard to all such arrangements, whether or not they involve the establishment of a separate entity, such as a pension scheme, superannuation scheme, or retirement benefit scheme, to receive contributions and to pay benefits.

28. Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan, as derived from its principal terms and conditions. In order to be classified as a defined contribution plan a post-employment benefit plan must require the entity to pay fixed contributions into a separate entity. Under defined contribution plans:

    (a) The entity's legal or constructive obligation is limited to the amount that it agrees to contribute to the fund. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions; and

    (b) In consequence, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall on the employee.

29. Examples of cases where an entity's obligation is not limited to the amount that it agrees to contribute to the fund are when the entity has a legal or constructive obligation through:

    (a) A plan benefit formula that is not linked solely to the amount of contributions;

(b) A guarantee, either indirectly through a plan or directly, of a specified return on contributions; or

(c) Those informal practices that give rise to a constructive obligation. For example, a constructive obligation may arise where an entity has a history of increasing benefits for former employees to keep pace with inflation, even where there is no legal obligation to do so.

30. Under defined benefit plans:

(a) The entity's obligation is to provide the agreed benefits to current and former employees; and

(b) Actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the entity. If actuarial or investment experience are worse than expected, the entity's obligation may be increased.

31. Unlike defined contribution plans, the definition of a defined benefit plan does not require the payment of contributions to a separate entity. Paragraphs 32–53 below explain the distinction between defined contribution plans and defined benefit plans in the context of multi-employer plans, state plans, composite social security programs, and insured benefits.

Multi-Employer Plans

32. **An entity shall classify a multi-employer plan as a defined contribution plan or a defined benefit plan under the terms of the plan (including any constructive obligation that goes beyond the formal terms). Where a multi-employer plan is a defined benefit plan, an entity shall:**

(a) **Account for its proportionate share of the defined benefit obligation, plan assets, and cost associated with the plan in the same way as for any other defined benefit plan; and**

(b) **Disclose the information required by paragraph 141.**

33. When sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an entity shall:

(a) **Account for the plan under paragraphs 55–57 as if it were a defined contribution plan;**

(b) **Disclose:**

(i) **The fact that the plan is a defined benefit plan; and**

(ii) **The reason why sufficient information is not available to enable the entity to account for the plan as a defined benefit plan; and**

(c) **To the extent that a surplus or deficit in the plan may affect the amount of future contributions, disclose in addition:**

(i) **Any available information about that surplus or deficit;**

(ii) **The basis used to determine that surplus or deficit; and**

(iii) **The implications, if any, for the entity.**

34. *One example of a defined benefit multi-employer plan is where:*

(a) The plan is financed on a pay-as-you-go basis, such that contributions of employers and/or employees are set at a level that is expected to be sufficient to pay the benefits falling due in the same period, and future benefits earned during the current period will be paid out of future contributions; and

(b) Employees' benefits are determined by the length of their service and the participating entities have no realistic means of withdrawing from the plan without paying a contribution for the benefits earned by employees up to the date of withdrawal.

Such a plan creates actuarial risk for the entity; if the ultimate cost of benefits already earned at the reporting date is more than expected, the entity will have to either increase its contributions or persuade employees to accept a reduction in benefits. Therefore, such a plan is a defined benefit plan.

35. Where sufficient information is available about a multi-employer plan that is a defined benefit plan, an entity accounts for its proportionate share of the defined benefit obligation, plan assets, and post-employment benefit cost associated with the plan in the same way as for any other defined benefit plan. However, there may be cases where an entity may not be able to identify its share of the underlying financial position and performance of the plan with sufficient reliability for accounting purposes. This may occur if:

(a) The entity does not have access to information about the plan that satisfies the requirements of this Standard; or

(b) The plan exposes the participating entities to actuarial risks associated with the current and former employees of other entities, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets, and cost to individual entities participating in the plan.

In those cases, an entity accounts for the plan as if it were a defined contribution plan, and discloses the additional information required by paragraph 33.

36. There may be a contractual agreement between the multi-employer plan and its participant entities that determines how the surplus in the plan will be distributed to the participant entities (or the deficit funded). A participant in a multi-employer plan with such an agreement that accounts for the plan as a defined contribution plan in accordance with paragraph 33 recognizes

the asset or liability that arises from the contractual agreement, and the resulting revenue or expense in surplus or deficit.

37. SLPSAS 8, *Provisions*, *Contingent Liabilities and Contingent Assets* requires an entity to disclose information about some contingent liabilities. In the context of a multi-employer plan, a contingent liability may arise from, for example:

(a) Actuarial losses relating to other participating entities because each entity that participates in a multi-employer plan shares in the actuarial risks of every other participating entity; or

(b) Any responsibility under the terms of a plan to finance any shortfall in the plan if other entities cease to participate.

38. Multi-employer plans are distinct from group administration plans. A group administration plan is merely an aggregation of single employer plans combined to allow participating employers to pool their assets for investment purposes and reduce investment management and administration costs, but the claims of different employers are segregated for the sole benefit of their own employees. Group administration plans pose no particular accounting problems because information is readily available to treat them in the same way as any other single employer plan and because such plans do not expose the participating entities to actuarial risks associated with the current and former employees of other entities. The definitions in this Standard require an entity to classify a group administration plan as a defined contribution plan or a defined benefit plan in accordance with the terms of the plan (including any constructive obligation that goes beyond the formal terms).

Defined Benefit Plans where the Participating Entities are under Common Control

39. Defined benefit plans that share risks between various entities under common control, for example, controlling and controlled entities, are not multi-employer plans.

40. An entity participating in such a plan obtains information about the plan as a whole, measured in accordance with this Standard on the basis of assumptions that apply to the plan as a whole. If there is a contractual agreement, binding arrangement, or stated policy for charging the net defined benefit cost for the plan as a whole measured in accordance with this Standard to individual entities within the economic entity, the entity shall, in its separate or individual financial statements, recognize the net defined benefit cost so charged. If there is no such agreement, arrangement, or policy, the net defined benefit cost shall be recognized in the financial statements of the entity that is legally the sponsoring employer for the plan. The other entities shall, in their financial statements, recognize a cost equal to their contribution payable for the period.

41. [Not used to maintain consistency of paragraph numbers with SLPSASs]

42. **Participation in such a plan is a related party transaction for each individual entity. An entity shall therefore, in its financial statements, make the following disclosures:**

    (a) **The contractual agreement, binding arrangement, or stated policy for charging the net defined benefit cost or the fact that there is no such policy.**

    (b) **The policy for determining the contribution to be paid by the entity.**

    (c) **If the entity accounts for an allocation of the net defined benefit cost in accordance with paragraph 40, all the information about the plan as a whole in accordance with paragraphs 140–142.**

    (d) **If the entity accounts for the contribution payable for the period in accordance with paragraph 40, the information about the plan as a whole required in accordance with paragraphs 141(b)–(e), (j), (n), (o), (q), and 142. The other disclosures required by paragraph 141 do not apply.**

State Plans

43. **An entity shall account for post-employment benefits under state plans in the same way as for a multi-employer plan (see paragraphs 32 and 33).**

44. State plans are established by legislation to cover all entities (or all entities in a particular category, for example, a specific industry) and are operated by national, state, or local government or by another body (for example, an agency created specifically for this purpose). This Standard deals only with employee benefits of the entity, and does not address accounting for any obligations under state plans related to employees and past employees of entities that are not controlled by the reporting entity. While governments may establish state plans and provide benefits to employees of private sector entities and/or self-employed individuals, obligations arising in respect of such plans are not addressed in this Standard.

45. Many state plans are funded on a pay-as-you-go basis: contributions are set at a level that is expected to be sufficient to pay the required benefits falling due in the same period; future benefits earned during the current period will be paid out of future contributions. Entities covered by state plans account for those plans as either defined contribution or defined benefit plans. The accounting treatment depends upon whether the entity has a legal or constructive obligation to pay future benefits. If an entity's only obligation is to pay the contributions as they fall due, and the entity has no obligation to pay future benefits, it accounts for that state plan as a defined contribution plan.

46. A state plan may be classified as a defined contribution plan by a controlled entity. However, it is a rebuttable presumption that the state plan will be characterized as a defined benefit plan by the controlling entity. Where that presumption is rebutted the state plan is accounted for as a defined contribution plan.

Composite Social Security Programs

47. **A reporting entity shall account for post-employment benefits under composite social security programs in the same way as for a multi-employer plan (see paragraphs 32 and 33).**

48. Composite social security programs are established by legislation and provide benefits to individuals who have satisfied eligibility criteria. Such criteria principally include a requirement that an individual has attained a retirement age laid down in legislation. There may also be other criteria related to factors such as income and personal wealth. In some jurisdictions, the composite social security program may also operate to provide benefits as consideration in exchange for employment services rendered by individuals. This Standard only addresses obligations in composite social security programs that arise as consideration in exchange for service rendered by employees and past employees of the reporting entity. This Standard requires a reporting entity to account for obligations for employee benefits that arise under composite social security programs as for a multi-employer plan in accordance with paragraphs 32 and 33.

49. For an economic entity, such as the whole-of-government level, the accounting treatment for obligations for employee benefits under composite social security programs depends upon whether the component of that program operating to provide post-employment benefits to employees of the economic entity is characterized as a defined contribution or a defined benefit plan. In making this judgment, the factors highlighted in paragraph 35 are considered.

Insured Benefits

50. **An entity may pay insurance premiums to fund a post-employment benefit plan. The entity shall treat such a plan as a defined contribution plan unless the entity will have (either directly or indirectly through the plan) a legal or constructive obligation to either:**

    (a) **Pay the employee benefits directly when they fall due; or**

    (b) **Pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.**

If the entity retains such a legal or constructive obligation, the entity shall treat the plan as a defined benefit plan.

51. The benefits insured by an insurance contract need not have a direct or automatic relationship with the entity's obligation for employee benefits. Post-employment benefit plans involving insurance contracts are subject to the same distinction between accounting and funding as other funded plans.

52. Where an entity funds a post-employment benefit obligation by contributing to an insurance policy under which the entity (either directly, indirectly through the plan, through the mechanism for setting future premiums, or through a related party relationship with the insurer) retains a legal or constructive obligation, the payment of the premiums does not amount to a defined contribution arrangement. It follows that the entity:

   (a) Accounts for a qualifying insurance policy as a plan asset (see paragraph 10); and

   (b) Recognizes other insurance policies as reimbursement rights (if the policies satisfy the criteria in paragraph 121).

53. Where an insurance policy (a) is in the name of a specified plan participant or a group of plan participants, and (b) the entity does not have any legal or constructive obligation to cover any loss on the policy, the entity has no obligation to pay benefits to the employees, and the insurer has sole responsibility for paying the benefits. The payment of fixed premiums under such contracts is, in substance, the settlement of the employee benefit obligation, rather than an investment to meet the obligation. Consequently, the entity no longer has an asset or a liability. Therefore, an entity treats such payments as contributions to a defined contribution plan.

Post-employment Benefits-Defined Contribution Plans

54. Accounting for defined contribution plans is straightforward because the reporting entity's obligation for each period is determined by the amounts to be contributed for that period. Consequently, no actuarial assumptions are required to measure the obligation or the expense, and there is no possibility of any actuarial gain or loss. Moreover, the obligations are measured on an undiscounted basis, except where they do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Recognition and Measurement

55. When an employee has rendered service to an entity during a period, the entity shall recognize the contribution payable to a defined contribution plan in exchange for that service:

(a) **As a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the reporting date, an entity shall recognize that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and**

(b) **As an expense, unless another Standard requires or permits the inclusion of the contribution in the cost of an asset (see, for example, SLPSAS 9 and SLPSAS 7.)**

56. **Where contributions to a defined contribution plan do not fall due wholly within twelve months after the end of the period in which the employees render the related service, they shall be discounted using the discount rate specified in paragraph 91.**

Disclosure

57. **An entity shall disclose the amount recognized as an expense for defined contribution plans.**

58. Where required by SLPSAS 14, an entity discloses information about contributions to defined contribution plans for key management personnel.

Post-employment Benefits-Defined Benefit Plans

59. Accounting for defined benefit plans is complex, because actuarial assumptions are required to measure the obligation and the expense, and there is a possibility of actuarial gains and losses. Moreover, the obligations are measured on a discounted basis, because they may be settled many years after the employees render the related service.

Recognition and Measurement

60. Defined benefit plans may be unfunded, or they may be wholly or partly funded by contributions by an entity, and sometimes its employees, into an entity or fund that is legally separate from the reporting entity and from which the employee benefits are paid. The payment of funded benefits when they fall due depends not only on the financial position and the investment performance of the fund but also on an entity's ability (and willingness) to make good any shortfall in the fund's assets. Therefore, the entity is, in substance, underwriting the actuarial and investment risks associated with the plan. Consequently, the expense recognized for a defined benefit plan is not necessarily the amount of the contribution due for the period.

61. Accounting by an entity for defined benefit plans involves the following steps:

(a) Using actuarial techniques to make a reliable estimate of the amount of benefit that employees have earned in return for their service in the current and prior periods. This requires an entity to determine how much benefit is attributable to the current and prior periods (see paragraphs 80–84), and to make estimates (actuarial assumptions) about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that will influence the cost of the benefit (see paragraphs 85–104);

(b) Discounting that benefit using the Projected Unit Credit Method in order to determine the present value of the defined benefit obligation and the current service cost (see paragraphs 77–79);

(c) Determining the fair value of any plan assets (see paragraphs 118–120);

(d) Determining the total amount of actuarial gains and losses and the amount of those actuarial gains and losses to be recognized (see paragraphs 105–111);

(e) Where a plan has been introduced or changed, determining the resulting past service cost (see paragraphs 112–117); and

(f) Where a plan has been curtailed or settled, determining the resulting gain or loss (see paragraphs 129–135). Where an entity has more than one defined benefit plan, the entity applies these procedures for each material plan separately. For example, a State Government responsible for educational and health services and a number of other services may have separate plans for teachers, healthcare workers, and other employees.

62. In some cases, estimates, averages, and computational short cuts may provide a reliable approximation of the detailed computations illustrated in this Standard. The amount payable at the reporting date in terms of the Payment of Gratuity Act No 12 of 1983 if employees terminate employment on that date, without considering the requirement to complete the minimum period of service for entitlement of gratuity in terms of the said Act, may be considered as a reliable approximation of the present value of the defined benefit obligation at the reporting date on benefits payable on termination of employment in terms of the said Act.

Accounting for the Constructive Obligation

63. **An entity shall account not only for its legal obligation under the formal terms of a defined benefit plan, but also for any constructive obligation that arises from the entity's informal practices. Informal practices give rise to a constructive obligation where the entity has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the entity's informal practices would cause unacceptable damage to its relationship with employees.**

64. The formal terms of a defined benefit plan may permit an entity to terminate its obligation under the plan. Nevertheless, it is usually difficult

for an entity to cancel a plan if employees are to be retained. Therefore, in the absence of evidence to the contrary, accounting for post-employment benefits assumes that an entity that is currently promising such benefits will continue to do so over the remaining working lives of employees.

Statement of Financial Position

65. **The amount recognized as a defined benefit liability shall be the net total of the following amounts:**

    (a) **The present value of the defined benefit obligation at the reporting date (see paragraph 77);**

    (b) **Plus any actuarial gains (less any actuarial losses) not recognized because of the treatment set out in paragraphs 105 and 106;**

    (c) **Minus any past service cost not yet recognized (see paragraph 112); and**

    (d) **Minus the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 118–120)**.

66. The present value of the defined benefit obligation is the gross obligation, before deducting the fair value of any plan assets.

67. **An entity shall determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognized in the financial statements do not differ materially from the amounts that would be determined at the reporting date.**

68. This Standard encourages, but does not require, an entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. For practical reasons, an entity may request a qualified actuary to carry out a detailed valuation of the obligation before the reporting date. Nevertheless, the results of that valuation are updated for any material transactions and other material changes in circumstances (including changes in market prices and interest rates) up to the reporting date.

69. **The amount determined under paragraph 65 may be negative (an asset). An entity shall measure the resulting asset at the lower of:**

    (a) **The amount determined under paragraph 65; and**

    (b) **The total of:**

        (i) **Any cumulative unrecognized net actuarial losses and past service cost (see paragraphs 105, 106 and 112); and**

        (ii) **The present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan. The present value of these**

economic benefits shall be determined using the discount rate specified in paragraph 91.

70. **The application of paragraph 69 shall not result in a gain being recognized solely as a result of an actuarial loss or past service cost in the current period, or in a loss being recognized solely as a result of an actuarial gain in the current period. The entity shall therefore recognize immediately under paragraph 65 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 69(b):**

    (a) **Net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 69(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period shall be recognized immediately under paragraph 65.**

    (b) **Net actuarial gains of the current period after the deduction of past service cost of the current period, to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 69(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period shall be recognized immediately under paragraph 65.**

71. Paragraph 70 applies to an entity only if it has, at the beginning or end of the accounting period, a surplus in a defined benefit plan and cannot, based on the current terms of the plan, recover that surplus fully through refunds or reductions in future contributions. In such cases, past service cost and actuarial losses that arise in the period, the recognition of which is deferred under paragraph 65, will increase the amount specified in paragraph 69(b)(i). If that increase is not offset by an equal decrease in the present value of economic benefits that qualify for recognition under paragraph 69(b)(ii), there will be an increase in the net total specified by paragraph 69(b) and, hence, a recognized gain. Paragraph 70 prohibits the recognition of a gain in these circumstances. The opposite effect arises with actuarial gains that arise in the period, the recognition of which is deferred under paragraph 65, to the extent that the actuarial gains reduce cumulative unrecognized actuarial losses. Paragraph 70 prohibits the recognition of a loss in these circumstances. For examples of the application of this paragraph, see Illustrative Examples, paragraphs IE8–IE30.

A surplus is an excess of the fair value of the plan assets over the present value of the defined benefit obligation.

72. An asset may arise where a defined benefit plan has been overfunded, or in certain cases where actuarial gains are recognized. An entity recognizes an asset in such cases because:

 (a) The entity controls a resource, which is the ability to use the surplus to generate future benefits;

 (b) That control is a result of past events (contributions paid by the entity and service rendered by the employee); and

 (c) Future economic benefits are available to the entity in the form of a reduction in future contributions or a cash refund, either directly to the entity or indirectly to another plan in deficit.

73. The limit in paragraph 69(b) does not override the delayed recognition of certain actuarial losses (see paragraphs 105 and 106) and certain past service cost (see paragraph 112), other than as specified in paragraph 70. Paragraph 141(f)(iii) requires an entity to disclose any amount not recognized as an asset because of the limit in paragraph 69(b).

Statement of Financial Performance

74. **An entity shall recognize the net total of the following amounts in surplus or deficit, except to the extent that another Standard requires or permits their inclusion in the cost of an asset:**

 (a) **Current service cost (see paragraphs 76–104);**

 (b) **Interest cost (see paragraph 95);**

 (c) **The expected return on any plan assets (see paragraphs 125–127) and on any reimbursement rights (see paragraph 121);**

 (d) **Actuarial gains and losses, as required in accordance with the entity's accounting policy (see paragraphs 105–109);**

 (e) **Past service cost (see paragraph 112);**

 (f) **The effect of any curtailments or settlements (see paragraphs 129 and 130); and**

 (g) **The effect of the limit in paragraph 69(b), unless it is recognized in the Statement of Changes in Net Assets/Equity in accordance with paragraph 108.**

75. Other Standards require the inclusion of certain employee benefit costs within the cost of assets, such as inventories or property, plant, and equipment (see SLPSAS 9 and SLPSAS 7). Any post-employment benefit costs included in the cost of such assets include the appropriate proportion of the components listed in paragraph 74.

Recognition and Measurement-Present Value of Defined Benefit Obligations and Current Service Cost

76. The ultimate cost of a defined benefit plan may be influenced by many variables, such as final salaries, employee turnover and mortality, medical cost trends and, for a funded plan, the investment earnings on the plan assets. The ultimate cost of the plan is uncertain and this uncertainty is likely to persist over a long period of time. In order to measure the present value of the post-employment benefit obligations and the related current service cost, it is necessary to:

    (a) Apply an actuarial valuation method (see paragraphs 77–79);

    (b) Attribute benefit to periods of service (see paragraphs 80–84); and

    (c) Make actuarial assumptions (see paragraphs 85–104).

Actuarial Valuation Method

77. **An entity shall use the Projected Unit Credit Method to determine the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost.**

78. The Projected Unit Credit Method (sometimes known as the accrued benefit method prorated on service or as the benefit/years of service method) sees each period of service as giving rise to an additional unit of benefit entitlement (see paragraphs 80–84), and measures each unit separately to build up the final obligation (see paragraphs 85–104).

79. An entity discounts the whole of a post-employment benefit obligation, even if part of the obligation falls due within twelve months of the reporting date.

Attributing Benefit to Periods of Service

80. **In determining the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost, an entity shall attribute benefit to periods of service under the plan's benefit formula. However, if an employee's service in later years will lead to a materially higher level of benefit than in earlier years, an entity shall attribute benefit on a straight-line basis from:**

    (a) The date when service by the employee first leads to benefits under the plan (whether or not the benefits are conditional on further service); until

    (b) The date when further service by the employee will lead to no material amount of further benefits under the plan, other than from further salary increases.

81. The Projected Unit Credit Method requires an entity to attribute benefit to the current period (in order to determine current service cost) and the current

and prior periods (in order to determine the present value of defined benefit obligations). An entity attributes benefit to periods in which the obligation to provide post-employment benefits arises. That obligation arises as employees render services in return for post-employment benefits that an entity expects to pay in future reporting periods. Actuarial techniques allow an entity to measure that obligation with sufficient reliability to justify recognition of a liability.

82. Employee service gives rise to an obligation under a defined benefit plan even if the benefits are conditional on future employment (in other words, they are not vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive reporting date, the amount of future service that an employee will have to render before becoming entitled to the benefit is reduced. In measuring its defined benefit obligation, an entity considers the probability that some employees may not satisfy any vesting requirements. Similarly, although certain post-employment benefits, for example, post-employment medical benefits, become payable only if a specified event occurs when an employee is no longer employed, an obligation is created when the employee renders service that will provide entitlement to the benefit if the specified event occurs. The probability that the specified event will occur affects the measurement of the obligation, but does not determine whether the obligation exists.

83. The obligation increases until the date when further service by the employee will lead to no material amount of further benefits. Therefore, all benefit is attributed to periods ending on or before that date. Benefit is attributed to individual accounting periods under the plan's benefit formula. However, if an employee's service in later years will lead to a materially higher level of benefit than in earlier years, n entity attributes benefit on a straight-line basis until the date when further service by the employee will lead to no material amount of further benefits. That is because the employee's service throughout the entire period will ultimately lead to benefit at that higher level.

84. Where the amount of a benefit is a constant proportion of final salary for each year of service, future salary increases will affect the amount required to settle the obligation that exists for service before the reporting date, but do not create an additional obligation. Therefore:

(a) For the purpose of paragraph 80(b), salary increases do not lead to further benefits, even though the amount of the benefits is dependent on final salary; and

(b) The amount of benefit attributed to each period is a constant proportion of the salary to which the benefit is linked.

Actuarial Assumptions

85. **Actuarial assumptions shall be unbiased and mutually compatible.**

86. Actuarial assumptions are an entity's best estimates of the variables that will determine the ultimate cost of providing post-employment benefits. Actuarial assumptions comprise:

  (a) Demographic assumptions about the future characteristics of current and former employees (and their dependants) who are eligible for benefits. Demographic assumptions deal with matters such as:

    (i) Mortality, both during and after employment;

    (ii) Rates of employee turnover, disability, and early retirement;

    (iii) The proportion of plan members with dependants who will be eligible for benefits; and

    (iv) Claim rates under medical plans.

  (b) Financial assumptions, dealing with items such as:

    (i) The discount rate (see paragraphs 91–95);

    (ii) Future salary and benefit levels (see paragraphs 96–100);

    (iii) In the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments (see paragraphs 101–104); and

    (iv) The expected rate of return on plan assets (see paragraphs 125–127).

87. Actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative.

88. Actuarial assumptions are mutually compatible if they reflect the economic relationships between factors such as inflation, rates of salary increase, the return on plan assets, and discount rates. For example, all assumptions that depend on a particular inflation level (such as assumptions about interest rates and salary and benefit increases) in any given future period assume the same inflation level in that period.

89. An entity determines the discount rate and other financial assumptions in nominal (stated) terms, unless estimates in real (inflation-adjusted) terms are more reliable, for example, in a hyperinflationary economy, or where the benefit is index-linked, and there is a deep market in index-linked bonds of the same currency and term.

90. **Financial assumptions shall be based on market expectations, at the reporting date, for the period over which the obligations are to be settled.**

Actuarial Assumptions-Discount Rate

91. **The rate used to discount post-employment benefit obligations (both funded and unfunded) shall reflect the time value of money. The currency and term of the financial instrument selected to reflect the time value of money shall be consistent with the currency and estimated term of the post-employment benefit obligations.**

92. One actuarial assumption that has a material effect is the discount rate. The discount rate reflects the time value of money but not the actuarial or investment risk. Furthermore, the discount rate does not reflect the entity-specific credit risk borne by the entity's creditors, nor does it reflect the risk that future experience may differ from actuarial assumptions.

93. The discount rate reflects the estimated timing of benefit payments. In practice, an entity often achieves this by applying a single weighted average discount rate that reflects the estimated timing and amount of benefit payments, and the currency in which the benefits are to be paid.

94. An entity makes a judgment whether the discount rate that reflects the time value of money is best approximated by reference to market yields at the reporting date on government bonds, high quality corporate bonds, or by another financial instrument. In some jurisdictions, market yields at the reporting date on government bonds will provide the best approximation of the time value of money. However, there may be jurisdictions in which this is not the case, for example, jurisdictions where there is no deep market in government bonds, or in which market yields at the reporting date on government bonds do not reflect the time value of money. In such cases, the reporting entity determines the rate by another method, such as by reference to market yields on high quality corporate bonds. There may also be circumstances where there is no deep market in government bonds or high quality corporate bonds with a sufficiently long maturity to match the estimated maturity of all the benefit payments. In such circumstances, an entity uses current market rates of the appropriate term to discount shorter term payments, and estimates the discount rate for longer maturities by extrapolating current market rates along the yield curve. The total present value of a defined benefit obligation is unlikely to be particularly sensitive to the discount rate applied to the portion of benefits that is payable beyond the final maturity of the available financial instrument, such as government bonds or corporate bonds.

95. Interest cost is computed by multiplying the discount rate as determined at the start of the period by the present value of the defined benefit obligation throughout that period, taking account of any material changes in the obligation. The present value of the obligation will differ from the liability recognized in the statement of financial position, (a) because the liability is recognized after deducting the fair value of any plan assets, and (b) because some actuarial gains and losses, and some past service cost, are not recognized immediately. The Illustrative Examples, paragraphs IE1–IE6, illustrate the computation of interest cost, among other things.

Actuarial Assumptions-Salaries, Benefits and Medical Costs

96. **Post-employment benefit obligations shall be measured on a basis that reflects:**

    (a) **Estimated future salary increases;**

    (b) **The benefits set out in the terms of the plan (or resulting from any constructive obligation that goes beyond those terms) at the reporting date; and**

    (c) **Estimated future changes in the level of any state benefits that affect the benefits payable under a defined benefit plan, if, and only if, either:**

        (i) **Those changes were enacted before the reporting date; or**

        (ii) **Past history, or other reliable evidence, indicates that those state benefits will change in some predictable manner, for example, in line with future changes in general price levels or general salary levels.**

97. Estimates of future salary increases take account of inflation, seniority, promotion, and other relevant factors, such as supply and demand in the employment market.

98. If the formal terms of a plan (or a constructive obligation that goes beyond those terms) require an entity to change benefits in future periods, the measurement of the obligation reflects those changes. This is the case when, for example:

    (a) The entity has a past history of increasing benefits, for example, to mitigate the effects of inflation, and there is no indication that this practice will change in the future; or

    (b) Actuarial gains have already been recognized in the financial statements, and the entity is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants (see paragraph 114(c)).

99. Actuarial assumptions do not reflect future benefit changes that are not set out in the formal terms of the plan (or a constructive obligation) at the reporting date. Such changes will result in:

    (a) Past service cost, to the extent that they change benefits for service before the change; and

    (b) Current service cost for periods after the change, to the extent that they change benefits for service after the change.

100. Some post-employment benefits are linked to variables, such as the level of benefit entitlements from social security pensions or state medical

care. The measurement of such benefits reflects expected changes in such variables, based on past history and other reliable evidence.

101. **Assumptions about medical costs shall take account of estimated future changes in the cost of medical services, resulting from both inflation and specific changes in medical costs.**

102. Measurement of post-employment medical benefits requires assumptions about the level and frequency of future claims and the cost of meeting those claims. An entity estimates future medical costs on the basis of historical data about the entity's own experience, supplemented where necessary by historical data from other entities, insurance companies, medical providers, or other sources. Estimates of future medical costs consider the effect of technological advances, changes in health care utilization or delivery patterns, and changes in the health status of plan participants.

103. The level and frequency of claims is particularly sensitive to the age, health status, and gender of employees (and their dependants), and may be sensitive to other factors such as geographical location. Therefore, historical data is adjusted to the extent that the demographic mix of the population differs from that of the population used as a basis for the historical data. It is also adjusted where there is reliable evidence that historical trends will not continue.

104. Some post-employment health care plans require employees to contribute to the medical costs covered by the plan. Estimates of future medical costs take account of any such contributions, based on the terms of the plan at the reporting date (or based on any constructive obligation that goes beyond those terms.) Changes in those employee contributions result in past service cost or, where applicable, curtailments. The cost of meeting claims may be reduced by benefits from state or other medical providers (see paragraphs 96(c) and 100.)

Actuarial Gains and Losses

105. **In measuring its defined benefit liability in accordance with paragraph 65, an entity shall, subject to paragraph 70, recognize a portion (as specified in paragraph 106) of its actuarial gains and losses as revenue or expense if the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded the greater of:**

(a) **10% of the present value of the defined benefit obligation at that date (before deducting plan assets); and**

(b) **10% of the fair value of any plan assets at that date.**

These limits shall be calculated and applied separately for each defined benefit plan.

106. **The portion of actuarial gains and losses to be recognized for each defined benefit plan is the excess determined in accordance with**

paragraph 105, divided by the expected average remaining working lives of the employees participating in that plan. However, an entity may adopt any systematic method that results in faster recognition of actuarial gains and losses, provided that the same basis is applied to both gains and losses, and the basis is applied consistently from period to period. An entity may apply such systematic methods to actuarial gains and losses even if they are within the limits specified in paragraph 105.

107. **If, as permitted by paragraph 106, an entity adopts a policy of recognizing actuarial gains and losses in the period in which they occur, it may recognize them as a separate item directly in net assets/equity, in accordance with paragraphs 108 and 109, providing it does so for:**

(a) **All of its defined benefit plans; and**

(b) **All of its actuarial gains and losses.**

108. Actuarial gains and losses recognized directly in net assets/equity as permitted by paragraph 107 shall be presented in the statement of changes in net assets/equity in accordance with paragraph 118(b) of SLPSAS 1.

109. An entity that recognizes actuarial gains and losses in accordance with paragraph 107 shall also recognize any adjustments arising from the limit in paragraph 69(b) outside surplus or deficit in the statement of changes in net assets/equity, in accordance with paragraph 118(b) of SLPSAS 1. Actuarial gains and losses and adjustments arising from the limit in paragraph 69(b) that have been recognized directly in the statement of changes in net assets/equity shall be recognized immediately in accumulated surpluses or deficits. They shall not be recognized in surplus or deficit in a subsequent period.

110. Actuarial gains and losses may result from increases or decreases in either the present value of a defined benefit obligation or the fair value of any related plan assets. Causes of actuarial gains and losses include, for example:

(a) Unexpectedly high or low rates of employee turnover, early retirement or mortality, or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases), or medical costs;

(b) The effect of changes in estimates of future employee turnover, early retirement, or mortality, or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases), or medical costs;

(c) The effect of changes in the discount rate; and

(d) Differences between the actual return on plan assets and the expected return on plan assets (see paragraphs 125–127).

111. In the long term, actuarial gains and losses may offset one another. Therefore, estimates of post-employment benefit obligations may be viewed as a range (or corridor) around the best estimate. An entity is permitted, but not required, to recognize actuarial gains and losses that fall within that range. This Standard requires an entity to recognize, as a minimum, a specified portion of the actuarial gains and losses that fall outside a corridor of plus or minus 10%. The Illustrative Examples, paragraphs IE1–IE6, illustrate the treatment of actuarial gains and losses, among other things. The Standard also permits systematic methods of faster recognition, provided that those methods satisfy the conditions set out in paragraph 106. Such permitted methods include, for example, immediate recognition of all actuarial gains and losses, both within and outside the corridor.

Past Service Cost

112. **In measuring its defined benefit liability under paragraph 65, an entity shall, subject to paragraph 70, recognize past service cost as an expense on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately following the introduction of, or changes to, a defined benefit plan, an entity shall recognize past service cost immediately.**

113. Past service cost arises when an entity introduces a defined benefit plan that attributes benefits to past service or changes the benefits payable for past service under an existing defined benefit plan. Such changes are in return for employee service over the period until the benefits concerned are vested. Therefore, the entity recognizes past service cost over that period, regardless of the fact that the cost refers to employee service in previous periods. The entity measures past service cost as the change in the liability resulting from the amendment (see paragraph 77). Negative past service cost arises when an entity changes the benefits attributable to past service so that the present value of the defined benefit obligation decreases.

114. Past service cost excludes:

(a) The effect of differences between actual and previously assumed salary increases on the obligation to pay benefits for service in prior years (there is no past service cost because actuarial assumptions allow for projected salaries);

(b) Under and over estimates of discretionary pension increases when an entity has a constructive obligation to grant such increases (there is no past service cost because actuarial assumptions allow for such increases);

(c) Estimates of benefit improvements that result from actuarial gains that have been recognized in the financial statements if the entity is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants, even if the benefit increase has not yet been formally awarded (the resulting increase in the obligation is an actuarial loss and not past service cost, see paragraph 98(b));

(d) The increase in vested benefits when, in the absence of new or improved benefits, employees complete vesting requirements (there is no past service cost because the entity recognized the estimated cost of benefits as current service cost as the service was rendered); and

(e) The effect of plan amendments that reduce benefits for future service (a curtailment).

115. An entity establishes the amortization schedule for past service cost when the benefits are introduced or changed. It would be impracticable to maintain the detailed records needed to identify and implement subsequent changes in that amortization schedule. Moreover, the effect is likely to be material only where there is a curtailment or settlement. Therefore, an entity amends the amortization schedule for past service cost only if there is a curtailment or settlement.

116. Where an entity reduces benefits payable under an existing defined benefit plan, the resulting reduction in the defined benefit liability is recognized as (negative) past service cost over the average period until the reduced portion of the benefits becomes vested.

117. Where an entity reduces certain benefits payable under an existing defined benefit plan and, at the same time, increases other benefits payable under the plan for the same employees, the entity treats the change as a single net change.

Recognition and Measurement-Plan Assets

Fair Value of Plan Assets

118. The fair value of any plan assets is deducted in determining the amount recognized in the statement of financial position under paragraph 65. When no market price is available, the fair value of plan assets is estimated, for example, by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligation).

119. Plan assets exclude unpaid contributions due from the reporting entity to the fund, as well as any non-transferable financial instruments issued by the entity and held by the fund. Plan assets are reduced by any liabilities of the fund that do not relate to employee benefits, for example, trade and other payables and liabilities resulting from derivative financial instruments.

120. Where plan assets include qualifying insurance policies that exactly match the amount and timing of some or all of the benefits payable under the

plan, the fair value of those insurance policies is deemed to be the present value of the related obligations, as described in paragraph 65 (subject to any reduction required if the amounts receivable under the insurance policies are not recoverable in full).

Reimbursements

121. **When, and only when, it is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, an entity shall recognize its right to reimbursement as a separate asset. The entity shall measure the asset at fair value. In all other respects, an entity shall treat that asset in the same way as plan assets. In the statement of financial performance, the expense relating to a defined benefit plan may be presented net of the amount recognized for a reimbursement.**

122. Sometimes, an entity is able to look to another party, such as an insurer, to pay part or all of the expenditure required to settle a defined benefit obligation. Qualifying insurance policies, as defined in paragraph 10, are plan assets. An entity accounts for qualifying insurance policies in the same way as for all other plan assets, and paragraph 121 does not apply (see paragraphs 50–53 and 120).

123 When an insurance policy is not a qualifying insurance policy, that insurance policy is not a plan asset. Paragraph 121 deals with such cases: the entity recognizes its right to reimbursement under the insurance policy as a separate asset, rather than as a deduction in determining the defined benefit liability recognized under paragraph 65; in all other respects, the entity treats that asset in the same way as plan assets. In particular, the defined benefit liability recognized under paragraph 65 is increased (reduced) to the extent that net cumulative actuarial gains (losses) on the defined benefit obligation and on the related reimbursement right remain unrecognized under paragraphs 105 and 106. Paragraph 141(f)(iv) requires the entity to disclose a brief description of the link between the reimbursement right and the related obligation.

124. If the right to reimbursement arises under an insurance policy or a legally binding agreement that exactly matches the amount and timing of some or all of the benefits payable under a defined benefit plan, the fair value of the reimbursement right is deemed to be the present value of the related obligation, as described in paragraph 65 (subject to any reduction required if the reimbursement is not recoverable in full).

Return on Plan Assets

125. The expected return on plan assets is one component of the expense recognized in the statement of financial performance. The difference between the expected return on plan assets and the actual return on plan assets is an actuarial gain or loss; it is included with the actuarial gains and losses on the defined benefit obligation in determining the net amount that is compared with the limits of the 10% corridor specified in paragraph 105.

126. The expected return on plan assets is based on market expectations, at the beginning of the period, for returns over the entire life of the related obligation. The expected return on plan assets reflects changes in the fair value of plan assets held during the period as a result of actual contributions paid into the fund and actual benefits paid out of the fund.

127. In determining the expected and actual return on plan assets, an entity deducts expected administration costs, other than those included in the actuarial assumptions used to measure the obligation.

Entity Combinations

128. In determining the assets and liabilities to be recognized related to post-employment benefits in an entity combination, an entity considers the Sri Lanka Accounting Standard dealing with entity combinations.

Curtailments and Settlements

129. **An entity shall recognize gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss on a curtailment or settlement shall comprise:**

   (a) **Any resulting change in the present value of the defined benefit obligation;**

   (b) **Any resulting change in the fair value of the plan assets; and**

   (c) **Any related actuarial gains and losses and past service cost that, under paragraphs 105 and 112, had not previously been recognized.**

130. **Before determining the effect of a curtailment or settlement, an entity shall remeasure the obligation (and the related plan assets, if any) using current actuarial assumptions (including current market interest rates and other current market prices).**

131. A curtailment occurs when an entity either:

   (a) Is demonstrably committed to make a significant reduction in the number of employees covered by a plan; or

   (b) Amends the terms of a defined benefit plan so that a significant element of future service by current employees will no longer qualify for benefits, or will qualify only for reduced benefits.

A curtailment may arise from an isolated event, such as the closing of a plant, discontinuance of an operation or termination or suspension of a plan, or a reduction in the extent to which future salary increases are linked to the benefits payable for past service. Curtailments are often linked with a restructuring. When this is the case, an entity accounts for a curtailment at the same time as for a related restructuring.

131A. When a plan amendment reduces benefits, only the effect of the reduction for future service is a curtailment. The effect of any reduction for past service is a negative past service cost.

132. A settlement occurs when an entity enters into a transaction that eliminates all further legal or constructive obligation for part or all of the benefits provided under a defined benefit plan, for example, when a lump-sum cash payment is made to, or on behalf of, plan participants in exchange for their rights to receive specified post-employment benefits.

133. In some cases, an entity acquires an insurance policy to fund some or all of the employee benefits relating to employee service in the current and prior periods. The acquisition of such a policy is not a settlement if the entity retains a legal or constructive obligation (see paragraph 50) to pay further amounts if the insurer does not pay the employee benefits specified in the insurance policy. Paragraphs 121–124 deal with the recognition and measurement of reimbursement rights under insurance policies that are not plan assets.

134. A settlement occurs together with a curtailment if a plan is terminated such that the obligation is settled and the plan ceases to exist. However, the termination of a plan is not a curtailment or settlement if the plan is replaced by a new plan that offers benefits that are, in substance, identical.

135. Where a curtailment relates to only some of the employees covered by a plan, or where only part of an obligation is settled, the gain or loss includes a proportionate share of the previously unrecognized past service cost and actuarial gains and losses. The proportionate share is determined on the basis of the present value of the obligations before and after the curtailment or settlement, unless another basis is more rational in the circumstances. For example, it may be appropriate to apply any gain arising on a curtailment or settlement of the same plan to first eliminate any unrecognized past service cost relating to the same plan.

Presentation

Offset

136. **An entity shall offset an asset relating to one plan against a liability relating to another plan when, and only when, the entity:**

(a) **Has a legally enforceable right to use a surplus in one plan to settle obligations under the other plan; and**

(b) **Intends either to settle the obligations on a net basis, or to realize the surplus in one plan and settle its obligation under the other plan simultaneously.**

137. [Not used to maintain consistency of paragraph numbers with SLPSASs]

Current/Non-Current Distinction

138. Some entities distinguish current assets and liabilities from non current assets and liabilities. This Standard does not specify whether an entity should distinguish current and non current portions of assets and liabilities arising from post-employment benefits.

Financial Components of Post-employment Benefit Costs

139. This Standard does not specify whether an entity should present current service cost, interest cost, and the expected return on plan assets as components of a single item of revenue or expense on the face of the statement of financial performance.

Disclosure

140. **An entity shall disclose information that enables users of financial statements to evaluate the nature of its defined benefit plans and the financial effects of changes in those plans during the period.**

141. **An entity shall disclose the following information about defined benefit plans:**

(a) **The entity's accounting policy for recognizing actuarial gains and losses;**

(b) **A general description of the type of plan;**

(c) **A reconciliation of opening and closing balances of the present value of the defined benefit obligation showing separately, if applicable, the effects during the period attributable to each of the following:**

(i) **Current service cost;**

(ii) **Interest cost;**

(iii) **Contributions by plan participants;**

(iv) **Actuarial gains and losses;**

(v) **Foreign currency exchange rate changes on plans measured in a currency different from the entity's presentation currency;**

(vi) **Benefits paid;**

(vii) **Past service cost;**

(viii) **Entity combinations;**

(ix) **Curtailments; and**

(x) **Settlements.**

(d) **An analysis of the defined benefit obligation into amounts arising from plans that are wholly unfunded and amounts arising from plans that are wholly or partly funded;**

(e) **A reconciliation of the opening and closing balances of the fair value of plan assets, and of the opening and closing balances of any reimbursement right recognized as an asset in accordance with paragraph 121 showing separately, if applicable, the effects during the period attributable to each of the following:**

(i) **Expected return on plan assets;**

(ii) **Actuarial gains and losses;**

(iii) **Foreign currency exchange rate changes on plans measured in a currency different from the entity's presentation currency;**

(iv) **Contributions by the employer;**

(v) **Contributions by plan participants;**

(vi) **Benefits paid;**

(vii) **Entity combinations; and**

(viii) **Settlements.**

(f) **A reconciliation of the present value of the defined benefit obligation in (c) and the fair value of the plan assets in (e) to the assets and liabilities recognized in the statement of financial position, showing at least:**

(i) **The net actuarial gains or losses not recognized in the statement of financial position (see paragraph 105);**

(ii) **The past service cost not recognized in the statement of financial position (see paragraph 112);**

(iii) **Any amount not recognized as an asset, because of the limit in paragraph 69(b);**

(iv) **The fair value at the reporting date of any reimbursement right recognized as an asset in accordance with paragraph 121 (with a brief description of the link between the reimbursement right and the related obligation); and**

(v) **The other amounts recognized in the statement of financial position.**

(g) **The total expense recognized in the statement of financial performance for each of the following, and the line item(s) in which they are included:**

(i) **Current service cost;**

(ii) **Interest cost;**

(iii) **Expected return on plan assets;**

(iv) **Expected return on any reimbursement right recognized as an asset in accordance with paragraph 121;**

(v) **Actuarial gains and losses;**

(vi) **Past service cost;**

(vii) **The effect of any curtailment or settlement; and**

(viii) **The effect of the limit in paragraph 69(b).**

(h) **The total amount recognized in the statement of changes in net assets/equity for each of the following:**

(i) **Actuarial gains and losses; and**

(ii) **The effect of the limit in paragraph 69(b).**

(i) **For entities that recognize actuarial gains and losses in the statement of changes in net assets/equity in accordance with paragraph 107, the cumulative amount of actuarial gains and losses recognized in that statement;**

(j) **For each major category of plan assets, which shall include, but is not limited to, equity instruments, debt instruments, property, and all other assets, the percentage or amount that each major category constitutes of the fair value of the total plan assets;**

(k) **The amounts included in the fair value of plan assets for:**

(i) **Each category of the entity's own financial instruments; and**

(ii) **Any property occupied by, or other assets used by, the entity.**

(l) **A narrative description of the basis used to determine the overall expected rate of return on assets, including the effect of the major categories of plan assets;**

(m) **The actual return on plan assets, as well as the actual return on any reimbursement right recognized as an asset in accordance with paragraph 121;**

(n) **The principal actuarial assumptions used as at the reporting date, including, when applicable:**

(i) **The discount rates;**

(ii) **The basis on which the discount rate has been determined;**

(iii) **The expected rates of return on any plan assets for the periods presented in the financial statements;**

(iv) **The expected rates of return for the periods presented in the financial statements on any reimbursement right recognized as an asset in accordance with paragraph 121;**

(v) **The expected rates of salary increases (and of changes in an index or other variable specified in the formal or constructive terms of a plan as the basis for future benefit increases);**

(vi) **Medical cost trend rates; and**

(vii) **Any other material actuarial assumptions used.**

An entity shall disclose each actuarial assumption in absolute terms (for example, as an absolute percentage) and not just as a margin between different percentages or other variables;

(o) **The effect of an increase of one percentage point and the effect of a decrease of one percentage point in the assumed medical cost trend rates on:**

(i) **The aggregate of the current service cost and interest cost components of net periodic post-employment medical costs; and**

(ii) **The accumulated post-employment benefit obligation for medical costs.**

For the purposes of this disclosure, all other assumptions shall be held constant. For plans operating in a high inflation environment, the disclosure shall be the effect of a percentage increase or decrease in the assumed medical cost trend rate of a significance similar to one percentage point in a low inflation environment;

(p) **The amounts for the current annual period and previous four annual periods of:**

(i) **The present value of the defined benefit obligation, the fair value of the plan assets, and the surplus or deficit in the plan; and**

(ii) **The experience adjustments arising on:**

a. **The plan liabilities expressed either as (1) an amount, or (2) a percentage of the plan liabilities at the reporting date; and**

b. **The plan assets expressed either as (1) an amount, or (2) a percentage of the plan assets at the reporting date**.

(q) **The employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the annual period beginning after the reporting date.**

142. Paragraph 141(b) requires a general description of the type of plan. Such a description distinguishes, for example, flat salary pension plans from final salary pension plans, and from post-employment medical plans. The description of the plan includes informal practices that give rise to constructive obligations included in the measurement of the defined benefit obligation in accordance with paragraph 63. Further detail is not required.

143. When an entity has more than one defined benefit plan, disclosures may be made in total, separately for each plan, or in such groupings as are considered to be the most useful. It may be useful to distinguish groupings by criteria such as the following:

(a) The geographical location of the plans; or

(b) Whether plans are subject to materially different risks, for example, by distinguishing flat salary pension plans from final salary pension plans, and from post-employment medical plans.

When an entity provides disclosures in total for a grouping of plans, such disclosures are provided in the form of weighted averages or of relatively narrow ranges.

144. Paragraph 33 requires additional disclosures about multi employer defined benefit plans that are treated as if they were defined contribution plans.

145. Where required by SLPSAS 14, an entity discloses information about:

(a) Related party transactions with post-employment benefit plans; and

(b) Post-employment benefits for key management personnel.

146. Where required by SLPSAS 8, an entity discloses information about contingent liabilities arising from post-employment benefit obligations.

Other Long-Term Employee Benefits

147. Other long-term employee benefits may include, for example:

(a) Long-term compensated absences such as long service or sabbatical leave;

(b) Jubilee or other long service benefits;

(c) Long-term disability benefits;

(d) Bonuses and profit sharing payable twelve months or more after the end of the period in which the employees render the related service;

(e) Deferred compensation paid twelve months or more after the end of the period in which it is earned; and

(f) Compensation payable by the entity until an individual enters new employment.

148. The measurement of other long-term employee benefits is not usually subject to the same degree of uncertainty as the measurement of post-employment benefits. Furthermore, the introduction of, or changes to, other long-term employee benefits rarely causes a material amount of past service cost. For these reasons, this Standard requires a simplified method of accounting for other long-term employee benefits. This method differs from the accounting required for post-employment benefits as follows:

(a) Actuarial gains and losses are recognized immediately and no corridor is applied; and

(b) All past service cost is recognized immediately.

149. This Standard includes a rebuttable presumption that long-term disability payments are not usually subject to the same degree of uncertainty as the measurement of post-employment benefits. Where this presumption is rebutted, the entity considers whether some or all long-term disability payments should be accounted for in accordance with paragraphs 59–146.

Recognition and Measurement

150. **The amount recognized as a liability for other long-term employee benefits shall be the net total of the following amounts:**

(a) **The present value of the defined benefit obligation at the reporting date (see paragraph 77);**

(b) **Minus the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 118–120).**

In measuring the liability, an entity shall apply paragraphs 55–104, excluding paragraphs 65 and 74. An entity shall apply paragraph 121 in recognizing and measuring any reimbursement right.

151. **For other long-term employee benefits, an entity shall recognize the net total of the following amounts as expense or (subject to paragraph 69) revenue, except to the extent that another Standard requires or permits their inclusion in the cost of an asset:**

(a) **Current service cost (see paragraphs 76–104)**;

(b) **Interest cost (see paragraph 95)**;

(c) **The expected return on any plan assets (see paragraphs 125–127) and on any reimbursement right recognized as an asset (see paragraph 121);**

(d) **Actuarial gains and losses, which shall all be recognized immediately;**

(e) **Past service cost, which shall all be recognized immediately; and**

(f) **The effect of any curtailments or settlements (see paragraphs 129 and 130).**

152. One form of other long-term employee benefit is long-term disability benefit. If the level of benefit depends on the length of service, an obligation arises when the service is rendered. Measurement of that obligation reflects the probability that payment will be required, and the length of time for which payment is expected to be made. If the level of benefit is the same for any disabled employee regardless of years of service, the expected cost of those benefits is recognized when an event occurs that causes a long-term disability. Paragraph 149 highlights the possibility that long-term disability benefit payments may be subject to a higher degree of uncertainty than other long-term employee benefits.

Disclosure

153. Although this Standard does not require specific disclosures about other long-term employee benefits, other Standards may require disclosures; for example, where the expense resulting from such benefits is material, and so would require disclosure in accordance with SLPSAS 1. When required by SLPSAS 14, an entity discloses information about other long-term employee benefits for key management personnel.

Termination Benefits

154. This Standard deals with termination benefits separately from other employee benefits, because the event which gives rise to an obligation is the termination rather than employee service.

Recognition

155. **An entity shall recognize termination benefits as a liability and an expense when, and only when, the entity is demonstrably committed to either:**

(a) **Terminate the employment of an employee or group of employees before the normal retirement date; or**

(b) **Provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.**

156. **An entity is demonstrably committed to a termination when, and only when, the entity has a detailed formal plan for the termination, and is without realistic possibility of withdrawal. The detailed plan shall include, as a minimum:**

(a) **The location, function, and approximate number of employees whose services are to be terminated;**

(b) **The termination benefits for each job classification or function; and**

(c) **The time at which the plan will be implemented. Implementation shall begin as soon as possible and the period of time to complete implementation shall be such that material changes to the plan are not likely.**

157. An entity may be committed, (a) by legislation, (b) by contractual or other agreements with employees or their representatives, or (c) by a constructive obligation based on business practice, custom, or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits. Termination benefits are typically lump-sum payments, but sometimes also include:

(a) Enhancement of retirement benefits or of other post-employment benefits, either indirectly through an employee benefit plan or directly; and

(b) Salary until the end of a specified notice period if the employee renders no further service that provides economic benefits to the entity.

158. Some employee benefits are payable regardless of the reason for the employee's departure. The payment of such benefits is certain (subject to any vesting or minimum service requirements) but the timing of their payment is uncertain. Although such benefits are described in some countries as termination indemnities, or termination gratuities, they are post-employment benefits rather than termination benefits, and an entity accounts for them as post-employment benefits. Some entities provide a lower level of benefit for voluntary termination at the request of the employee (in substance, a post-employment benefit) than for involuntary termination at the request of the entity. The additional benefit payable on involuntary termination is a termination benefit.

159. Termination benefits do not provide an entity with future economic benefits, and are recognized as an expense immediately.

160. Where an entity recognizes termination benefits, the entity may also have to account for a curtailment of retirement benefits or other employee benefits (see paragraph 129).

Measurement

161. **Where termination benefits fall due more than 12 months after the reporting date, they shall be discounted using the discount rate specified in paragraph 91.**

162. **In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits shall be based on the number of employees expected to accept the offer**.

Disclosure

163. Where there is uncertainty about the number of employees who will accept an offer of termination benefits, a contingent liability exists. As required by SLPSAS 8, an entity discloses information about the contingent liability unless the possibility of an outflow in settlement is remote.

164. As required by SLPSAS 1, an entity discloses the nature and amount of an expense if it is material. Termination benefits may result in an expense needing disclosure in order to comply with this requirement.

165. Where required by SLPSAS 14, an entity discloses information about termination benefits for key management personnel.

First Time Adoption of this Standard

166. **On first adopting this Standard, an entity shall determine its initial liability for defined benefit plans at that date as:**
    - (a) **The present value of the obligations (see paragraph 77) at the date of adoption;**
    - (b) **Minus the fair value, at the date of adoption, of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 118–120);**
    - (c) **Minus any past service cost that, under paragraph 112, shall be recognized in later periods**.

167. **If the initial liability determined in accordance with paragraph 166 is more or less than the liability that would have been recognized at the same date under the entity's previous accounting policy, the entity shall recognize that increase/decrease in opening accumulated surpluses or deficits.**

168. On the initial adoption of this Standard, the effect of the change in accounting policy includes all actuarial gains and losses that arose in earlier periods, even if they fall inside the corridor specified in paragraph 105. Entities reporting under accrual accounting for the first time will not have recognized any liability, in which case the increase in the liability will represent the full amount of the liability minus the fair value, at the date of adoption, of any plan assets in accordance with paragraph 166(b) and any past service cost to be recognized in later periods in accordance with

paragraph 166(c). Under the provisions of this Standard, this increased liability is recognized in accumulated surpluses or deficits.

169. **On first adopting this Standard, an entity shall not split the cumulative actuarial gains and losses from the inception of the defined benefit plan(s) until the date of first adoption of this Standard into a recognized and unrecognized portion. All cumulative actuarial gains and losses shall be recognized in opening accumulated surpluses or deficits.**

170. On first adoption of this Standard, entities are not permitted to split cumulative actuarial gains and losses into recognized and unrecognized portions. All cumulative gains and losses are recognized in opening accumulated surpluses or deficits. This requirement on first-time adoption of this Standard does not preclude an entity electing to recognize only part of its actuarial gains and losses in accordance with the requirements in paragraphs 105–107 in subsequent reporting periods.

171. **In the first year of adoption of this Standard, an entity is not required to provide comparative information.**

172. Paragraph 171 provides relief from the inclusion of comparative information to all entities in the first year of adoption of this Standard. An entity is encouraged to include comparative information where this is available.

173. **In the first year of adoption of this Standard, an entity is not required to provide the disclosures in paragraphs 141(c), 141(e), and 141(f).**

174. The reconciliations in paragraphs 141(c) and 141(e) both involve the disclosure of opening balances relating to components of defined benefit obligations, plan assets, and reimbursement rights. The disclosure in paragraph 141(f) requires a reconciliation that relies on information in paragraphs 141(c) and 141(e). These disclosures are not required in the first year of adoption of this Standard. An entity is encouraged to include these disclosures where the information is available.

175. **In the first year of adoption of this Standard, an entity may provide the information required in paragraph 141(p) prospectively.**

176. The information specified in paragraph 141(p) relates to the present value of the defined benefit obligation, the fair value of the plan assets, the surplus or deficit in the plan, and certain experience adjustments. This disclosure is only required for the current annual period in the first year of adoption. Information on prior annual periods can be provided prospectively as the entity reports under the requirements of this Standard. This allows entities to build trend information over a period, rather than producing such information for reporting periods prior to the period of first adoption of the Standard.

Effective Date

177. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after January 1, 2018. Earlier adoption is encouraged. If an entity applies this Standard for a period beginning before January 1, 2018, it shall disclose that fact.**

178. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Application Guidance

This Appendix is an integral part of SLPSAS 19.

Example Illustrating Paragraph 21: Accounting for a Performance-Related Bonus Plan

AG1. A performance-related bonus plan requires a government printing unit to pay a specified proportion of its surplus for the year to employees who meet predetermined performance targets and serve throughout the year, i.e., are in post on both the first and last day of the reporting period. If no employees leave during the year, the total bonus payments for the year will be 3% of actual surplus. The entity determines that staff turnover will reduce the payments to 2.5% of actual surplus.

The entity recognizes a liability and an expense of 2.5% of actual surplus.

Example Illustrating Paragraph 36: Accounting for a Multi-Employer Plan

AG2. Along with similar entities in Province X, Local Government Unit A participates in a multi-employer defined benefit plan. Because the plan exposes the participating entities to actuarial risks associated with the current and former employees of other local government units participating in the plan, there is no consistent and reliable basis for allocating the obligation, plan assets, and cost to individual local government units participating in the plan. Local Government Unit A therefore accounts for the plan as if it were a defined contribution plan. A funding valuation, which is not drawn up on the basis of assumptions compatible with the requirements of this Standard, shows a deficit of 480 million rupees in the plan. The plan has agreed, under a binding arrangement, a schedule of contributions with the participating employers in the plan that will eliminate the deficit over the next five years. Local Government Unit A's total contributions under the contract are 40 million rupees.

The entity recognizes a liability for the contributions adjusted for the time value of money and an equal expense in surplus or deficit.

Example Illustrating Paragraph 73: Limits on Recognition of Plan Asset

AG3. A defined benefit plan has the following characteristics:

Present value of the obligation	1100
Fair value of plan assets	(1190)
	(90)
Unrecognized actuarial losses	(110)
Unrecognized past service cost	(70)
Negative amount determined under paragraph 65	(270)
Present value of available future refunds and reductions in future contributions	60
The limit under paragraph 69(b) is computed as follows:	
Unrecognized actuarial losses	*110*
Unrecognized past service cost	*70*
Present value of available future refunds and reductions in future contributions	*60*
Limit	*240*

240 is less than 270. Therefore, the entity recognizes an asset of 240 and discloses that the limit in paragraph 69(b) reduced the carrying amount of the asset by 30 (see paragraph 141(f)(iii)).

Example Illustrating Paragraph 78: Projected Unit Credit Method

AG4. A lump sum benefit is payable on termination of service and equal to 1% of final salary for each year of service. The salary in year 1 is 10,000 and is assumed to increase at 7% (compound) each year. The discount rate used is 10% per annum. The following table shows how the obligation builds up for an employee who is expected to leave at the end of year five, assuming that there are no changes in actuarial assumptions. For simplicity, this example ignores the additional adjustment needed to reflect the probability that the employee may leave the entity at an earlier or later date.

Year	*1*	*2*	*3*	*4*	*5*
Benefit attributed to:					
– prior years	*0*	*131*	*262*	*393*	*524*
– current year (1% of final salary)	*131*	*131*	*131*	*131*	*131*
– current and prior years	*131*	*262*	*393*	*524*	*655*
Year	*1*	*2*	*3*	*4*	*5*
Opening obligation	*–*	*8*	*196*	*324*	*476*
Interest at 10%	*–*	*9*	*20*	*33*	*48*
Current service cost	*89*	*98*	*108*	*119*	*131*
Closing obligation	*89*	*196*	*324*	*476*	*655*

Note:

1. *The opening obligation is the present value of benefit attributed to prior years.*
2. *The current service cost is the present value of benefit attributed to the current year.*
3. *The closing obligation is the present value of benefit attributed to current and prior years*

Examples Illustrating Paragraph 81: Attributing Benefit to Years of Service

AG5. A defined benefit plan provides a lump sum benefit of 100 payable on retirement for each year of service.

A benefit of 100 is attributed to each year. The current service cost is the present value of 100. The present value of the defined benefit obligation is the present value of 100, multiplied by the number of years of service up to the reporting date.

If the benefit is payable immediately when the employee leaves the entity, the current service cost and the present value of the defined benefit obligation reflect the date at which the employee is expected to leave. Thus, because of the effect of discounting, they are less than the amounts that would be determined if the employee left at the reporting date.

AG6. A plan provides a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65.

Benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.2% of the estimated final salary payable from the expected retirement date until the expected date of death is attributed to each year of service. The current service cost is the present value of that benefit. The present value of the defined benefit obligation is the present value of monthly pension payments of 0.2% of final salary, multiplied by the number of years of service up to the reporting date. The current service *cost and the present value of the defined benefit obligation are discounted, because pension payments begin at the age of 65.*

Examples Illustrating Paragraph 82: Vesting and Non-Vesting Benefits

AG7. A plan pays a benefit of 100 for each year of service. The benefits vest after 10 years of service.

A benefit of 100 is attributed to each year. In each of the first 10 years, the current service cost and the present value of the obligation reflect the probability that the employee may not complete ten years of service.

AG8. A plan pays a benefit of 100 for each year of service, excluding service before the age of 25. The benefits vest immediately.

No benefit is attributed to service before the age of 25, because service before that date does not lead to benefits (conditional or unconditional). A benefit of 100 is attributed to each subsequent year.

Examples Illustrating Paragraph 83: Attributing Benefits to Accounting Periods

AG9. A plan pays a lump sum benefit of 1,000 that vests after 10 years of service. The plan provides no further benefit for subsequent service.

A benefit of 100 (1,000 divided by 10) is attributed to each of the first 10 years. The current service cost in each of the first 10 years reflects the probability that the employee may not complete 10 years of service. No benefit is attributed to subsequent years.

AG10. A plan pays a lump sum retirement benefit of 2,000 to all employees who are still employed at the age of 55 after 20 years of service, or who are still employed at the age of 65, regardless of their length of service.

For employees who join before the age of 35, service first leads to benefits under the plan at the age of 35 (an employee could leave at the age of 30 and return at the age of 33, with no effect on the amount or timing of benefits). Those benefits are conditional on further service. Also, service beyond the age of 55 will lead to no material amount of further benefits. For these employees, the entity attributes benefit of 100 (2,000 divided by 20) to each year from the age of 35 to the age of 55.

For employees who join between the ages of 35 and 45, service beyond twenty years will lead to no material amount of further benefits. For these employees, the entity attributes benefit of 100 (2,000 divided by 20) to each of the first twenty years.

For an employee who joins at the age of 55, service beyond ten years will lead to no material amount of further benefits. For this employee, the entity attributes benefit of 200 (2,000 divided by 10) to each of the first 10 years.

For all employees, the current service cost and the present value of the obligation reflect the probability that the employee may not complete the necessary period of service.

AG11. A post-employment medical plan reimburses 40% of an employee's post-employment medical costs if the employee leaves after more than 10 and less than 20 years of service, and 50% of those costs if the employee leaves after 20 or more years of service.

Under the plan's benefit formula, the entity attributes 4% of the present value of the expected medical costs (40% divided by 10) to each of the first ten years and 1% (10% divided by 10) to each of the second 10 years. The current service cost in each year reflects the probability that the employee may not complete the necessary period of service to earn part or all of the benefits. For employees expected to leave within 10 years, no benefit is attributed.

AG12. A post-employment medical plan reimburses 10% of an employee's post-employment medical costs if the employee leaves after more than 10 and less than 20 years of service, and 50% of those costs if the employee leaves after 20 or more years of service.

Service in later years will lead to a materially higher level of benefit than in earlier years. Therefore, for employees expected to leave after 20 or more years, the entity attributes benefit on a straight-line basis under paragraph 68. Service beyond 20 years will lead to no material amount of further benefits. Therefore, the benefit attributed to each of the first 20 years is 2.5% of the present value of the expected medical costs (50% divided by 20).

For employees expected to leave between 10 and 20 years, the benefit attributed to each of the first 10 years is 1% of the present value of the expected medical costs. For these employees, no benefit is attributed to service between the end of the tenth year and the estimated date of leaving.

For employees expected to leave within 10 years, no benefit is attributed.

Example Illustrating Paragraph 84: Attributing Benefits to Accounting Periods

AG13. Employees are entitled to a benefit of 3% of final salary for each year of service before the age of 55.

Benefit of 3% of estimated final salary is attributed to each year up to the age of 55. This is the date when further service by the employee will lead to no material amount of further benefits under the plan. No benefit is attributed to service after that age.

Example Illustrating Paragraph 113: Accounting for Past Service Cost

AG14. An entity operates a pension plan that provides a pension of 2% of final salary for each year of service. The benefits become vested after five years of service. On January 1, 20X9, the entity improves the pension to 2.5% of final salary for each year of service starting from January 1, 20X5. At the date of the improvement, the present value of the additional benefits for service from January 1, 20X5 to January 1, 20X9 is as follows:

Employees with more than five years service at 1/1/X9	150
Employees with less than five years service at 1/1/X9 (average period until vesting: three years)	120
	270

The entity recognizes 150 immediately because those benefits are already vested. The entity recognizes 120 on a straight-line basis over three years from January 1, 20X9.

Example Illustrating Paragraphs 121–123: Reimbursements

AG15. Reimbursements:

Present value of obligation	1,241
Unrecognized actuarial gains	17
Liability recognized in statement of financial position	1,258
Rights from insurance policies that exactly match the amount and timing of some of the benefits payable under the plan. Those benefits have a present value of 1,092.	1,092

The unrecognized actuarial gains of 17 are the net cumulative actuarial gains on the obligation and on the reimbursement rights.

Example Illustrating Paragraph 125–127: Return on Plan Assets

AG16. At January 1, 20X7, the fair value of plan assets was 10,000, and net cumulative unrecognized actuarial gains were 760. On June 30, 20X7, the plan paid benefits of 1,900 and received contributions of 4,900. At December 31, 20X7, the fair value of plan assets was 15,000, and the present value of the defined benefit obligation was 14,792. Actuarial losses on the obligation for 20X7 were 60.

At January 1, 20X7, the reporting entity made the following estimates, based on market prices at that date:

	%
Interest and dividend income, after tax payable by the fund	9.25
Realized and unrealized gains on plan assets (after tax)	2.00
Administration costs	(1.00)
Expected rate of return	10.25

For 20X7, the expected and actual return on plan assets are as follows:

Return on 10,000 held for 12 months at 10.25%	1,025
Return on 3,000 held for six months at 5% (equivalent to 10.25% annually, compounded every six months)	150
Expected return on plan assets for 20X7	1,175
Fair value of plan assets at December 31, 20X7	15,000
Less fair value of plan assets at January 1, 20X7	(10,000)
Less contributions received	(4,900)
Add benefits paid	1,900
Actual return on plan assets	2,000

The difference between the expected return on plan assets (1,175) and the actual return on plan assets (2,000) is an actuarial gain of 825. Therefore, the cumulative net unrecognized actuarial gains are 1,525 (760 plus 825 minus 60). Under paragraph 105, the limits of the corridor are set at 1,500 (greater of: (i) 10% of 15,000 and (ii) 10% of 14,792). In the following year (20X8), the entity recognizes in surplus or deficit an actuarial gain of 25 (1,525 minus 1,500) divided by the expected average remaining working life of the employees concerned.

The expected return on plan assets for 20X8 will be based on market expectations at January 1 20X8 for returns over the entire life of the obligation.

Example Illustrating Paragraph 135: Accounting for a Curtailment Without a Settlement

AG17. An entity is required by legislation to discontinue the direct provision of waste collection and waste disposal services. Employees of this discontinued segment will earn no further benefits. This is a curtailment without a settlement. Using current actuarial assumptions (including current market interest rates and other current market prices) immediately before the curtailment, the entity has a defined benefit obligation with a net present value of 1,000, plan assets with a fair value of 820, and net cumulative unrecognized actuarial gains of 50. The curtailment reduces the net present value of the obligation by 100 to 900.

Of the previously unrecognized actuarial gains, 10% (100/1,000) relates to the part of the obligation that was eliminated through the curtailment. Therefore, the effect of the curtailment is as follows:

	Before Curtailment	*Curtailment gain*	*After Curtailment*
Net present value of obligation	*1000*	*(100)*	*900*
Fair value of plan assets	*(820)*	*-*	*(820)*
	180	*(100)*	*80*
Unrecognized actuarial gains	*50*	*(5)*	*45*
Net liability recognized in statement of financial position	*230*	*(105)*	*125*

Example Illustrating Paragraphs 166 to 168: Determining the Initial Liability

AG18. At December 31 2010, an entity's statement of financial position includes a pension liability of 100. The entity adopts this Standard as of January 1 2011, when the present value of the obligation under the Standard is 1,300 and the fair value of plan assets is 1,000. On January 1 2005, the entity had improved pensions (cost for non-vested benefits: 160; and average remaining period at that date until vesting: 10 years)

The initial effect is as follows:	
Present value of the obligation	*1,300*
Fair value of plan assets	*(1,000)*
Minus: past service cost to be recognized in later periods (160 × 4/10)	*(64)*
Initial liability	*236*
Liability already recognized under previous policy	*(100)*
Additional liability	*136*

The entity recognizes the additional liability of 136 in opening accumulated surpluses or deficits

Illustrative Examples

These examples accompany, but are not part of, SLPSAS 19.

Funded Defined Benefit Plan

Extracts from statements of financial performance and statements of financial position are provided to show the effects of the transactions described below. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Standards.

Background Information

IE1. The following information is given about a funded defined benefit plan. To keep interest computations simple, all transactions are assumed to occur at the year end. The present value of the obligation and the fair value of the plan assets were both 1,000 at January 1, 20X7. Net cumulative unrecognized actuarial gains at that date were 140.

	20X7	**20X8**	**20X9**
Discount rate at start of year	10.0%	9.0%	8.0%
Expected rate of return on plan assets at start of year	12.0%	11.1%	10.3%
Current service cost	130	140	150
Benefits paid	150	180	190
Contributions paid	90	100	110
Present value of obligation at December 31	1,141	1,197	1,295
Fair value of plan assets at December 31	1,092	1,109	1,093
Expected average remaining working lives of employees (years)	10	10	10

IE2. In 20X8, the plan was amended to provide additional benefits with effect from January 1, 20X8. The present value as at January 1, 20X8 of additional benefits for employee service before January 1, 20X8 was 50 for vested benefits and 30 for non-vested benefits. As at January 1, 20X8, the entity estimated that the average period until the non-vested benefits would become vested was three years; the past service cost arising from additional non-vested benefits is therefore recognized on a straight-line basis over three years. The past service cost arising from additional vested benefits is recognized immediately (paragraph 112 of the Standard). The entity has adopted a policy of recognizing actuarial gains and losses under the minimum requirements of paragraph 106.

Changes in the Present Value of the Obligation and in the Fair Value of the Plan Assets

IE3. The first step is to summarize the changes in the present value of the obligation and in the fair value of the plan assets and use this to determine the amount of the actuarial gains or losses for the period. These are as follows

	20x7	**20x8**	**20x9**
Present value of obligation, January1	1,000	1,141	1,197
Interest cost	100	103	96
Current service cost	130	140	150
Past service cost – non-vested benefits	–	30	–
Past service cost – vested benefits	–	50	–
Benefits paid	(150)	(180)	(190)
Actuarial (gain) loss on obligation (balancing figure)	61	(87)	42
Present value of obligation, December 31	1,141	1,197	1,295
Fair value of plan assets, January 1	1,000	1,092	1,109
Expected return on plan assets	120	121	114
Contributions	90	100	110
Benefits paid	(150)	(180)	(190)
Actuarial gain (loss) on plan assets (balancing figure)	32	(24)	(50)
Fair value of plan assets, December 31	1,092	1,109	1,093

Limits of the Corridor

IE4. The next step is to determine the limits of the corridor, and then compare these with the cumulative unrecognized actuarial gains and losses in order to determine the net actuarial gain or loss to be recognized in the following period. Under paragraph 105 of this Standard, the limits of the corridor are set at the greater of:

(a) 10% of the present value of the obligation before deducting plan assets; and

(b) 10% of the fair value of any plan assets.

IE5. These limits, and the recognized and unrecognized actuarial gains and losses, are as follows:

	20x7	**20x8**	**20x9**
Net cumulative unrecognized actuarial gains (losses) at January1	140	107	170
Limits of corridor at January 1	100	114	120
Excess [A]	40	–	50
Average expected remaining working lives (years) [B]	10	10	10
Actuarial gain (loss) to be recognized [A/B]	4	–	5
Unrecognized actuarial gains (losses) at January 1	140	107	170
Actuarial gain (loss) for year – obligation	(61)	87	(42)
Actuarial gain (loss) for year – plan assets	32	(24)	(50)
Subtotal	111	170	78
Actuarial (gain) loss recognized	(4)	–	(5)
Unrecognized actuarial gains (losses) at December 31	107	170	73

Amounts Recognized in the Statement of Financial Position and Statement of Financial Performance, and Related Analyses

IE6. The final step is to determine the amounts to be recognized in the statement of financial position and the statement of financial performance, and the related analyses to be disclosed in accordance with paragraph 141(f), (g), and (m) of the Standard (the analyses required to be disclosed in accordance with paragraph 141(c) and (e) are given in the section of this Illustrative Example, “Changes in the Present Value of the Obligation and in the Fair Value of the Plan Assets.” These are as follows.

	20x7	20x8	20x9
Present value of the obligation	1,141	1,197	1,295
Fair value of plan assets	(1,092)	(1,109)	(1,093)
	49	88	202
Unrecognized actuarial gains (losses)	107	170	73
Unrecognized past service cost – non-vested benefits	–	(20)	(10)
Liability recognized in statement of financial position	**156**	**238**	**265**
Current service cost	130	140	150
Interest cost	100	103	96
Expected return on plan assets	(120)	(121)	(114)
Net actuarial (gain) loss recognized in year	(4)	–	(5)
Past service cost – non-vested benefits	–	10	10
Past service cost – vested benefits	–	50	–
Expense recognized in statement of financial performance	**106**	**182**	**137**
Actual return on plan assets			
Expected return on plan assets	120	121	114
Actuarial gain (loss) on plan assets	32	(24)	(50)
Actual return on plan assets	152	97	64

Note: see example illustrating paragraphs 121–123 for presentation of reimbursements.

Disclosures

Extracts from notes show how the required disclosures may be aggregated in the case of an entity that provides a variety of employee benefits. These extracts do not necessarily conform with all the disclosure and presentation requirements of SLPSAS 19 and other standards. In particular, they do not illustrate the disclosure of:

(a) *Accounting policies for employee benefits (see SLPSAS 1, Presentation of Financial Statements.) Paragraph 141(a) of this Standard requires this disclosure to include the entity's accounting policy for recognizing actuarial gains and losses;*

(b) *A general description of the type of plan (paragraph 141(b));*

(c) *A narrative description of the basis used to determine the overall expected rate of return on assets (paragraph 141(l)).*

(d) *Employee benefits granted to key management personnel (see SLPSAS 14, Related Party Disclosures); or*

(e) *Share-based employee benefits (see the Sri Lanka Accounting Standard dealing with share-based payments).*

IE7. Illustrative disclosures are as follows.

Employee Benefit Obligations

The amounts recognized in the statement of financial position are as follows:

	Defiend benefit pension plans		**Post-employment medical benefits**	
	20x8	**20x7**	**20x8**	**20x7**
Present value of funded obligations	20,300	17,400	–	–
Fair value of plan assets	(18,420)	(17,280)	–	–
	1,880	120	–	–
Present value of unfunded obligations	2,000	1,000	7,337	6,405
Unrecognized actuarial gains (losses)	(1,605)	840	(2,707)	(2,607)
Unrecognized past service cost	(450)	(650)	–	–
Net liability	1,825	1,310	4,630	3,798
Amounts in the statement of financial position:				
liabilities	1,825	1,400	4,630	3,798
assets	–	(90)	–	–
Net liability	1,825	1,310	4,630	3,798

The pension plan assets include ordinary shares issued by [name of reporting entity] with a fair value of 317 (20X7: 281). Plan assets also include property occupied by [name of reporting entity] with a fair value of 200 (20X7: 185).

The amounts recognized in surplus or deficit are as follows:

	Defiend benefit pension plans		**Post-employment medical benefits**	
	20x8	**20x7**	**20x8**	**20x7**
Current service cost	850	750	479	411
Interest on obligation	950	1,000	803	705
Expected return on plan assets	(900)	(650)		
Net actuarial losses (gains) recognized in year	(70)	(20)	150	140
Past service cost	200	200		
Losses (gains) on curtailments and settlements	175	(390)		
Total, included in employee benefits expense	1,205	890	1,432	1,256
Actual return on plan assets	600	2,250	–	–

Changes in the present value of the defined benefit obligation are as follows:

	Defiend benefit pension plans		Post-employment medical benefits	
	20x8	20x7	20x8	20x7
Opening defined benefit obligation	18,400	11,600	6,405	5,439
Service cost	850	750	479	411
Interest cost	950	1,000	803	705
Actuarial losses (gains)	2,350	950	250	400
Losses (gains) on curtailments	(500)	–		
Liabilities extinguished on settlements	–	(350)		
Liabilities assumed in an entity combination	–	5,000		
Exchange differences on foreign plans	900	(150)		
Benefits paid	(650)	(400)	(600)	(550)
Closing defined benefit obligation	22,300	18,400	7,337	6,405

Changes in the fair value of plan assets are as follows

	Defiend benefit pension plans	
	20x8	20x7
Opening fair value of plan assets	17,280	9,200
Expected return	900	650
Actuarial gains (losses)	(300)	1,600
Assets distributed on settlements	(400)	–
Contributions by employer	700	350
Assets acquired in an entity combination	–	6,000
Exchange differences on foreign plans	890	(120)
Benefits paid	(650)	(400)
	18,420	17,280

The entity expects to contribute 900 to its defined benefit pension plans in 20X9.

The major categories of plan assets as a percentage of total plan assets are as follows:

	20x8	20x7
European equities	30%	35%
North American equities	16%	15%
European bonds	31%	28%
North American bonds	18%	17%
Property	5%	5%

Principal actuarial assumptions at the reporting date (expressed as weighted averages):

	20x8	20x7
Discount rate at December 31	5%	6.5%
Expected return on plan assets at December 31	5.4%	7%
Future salary increases	5%	4%
Future pension increases	3%	2%
Proportion of employees opting for early retirement	30%	30%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

Assumed healthcare cost trend rates have a significant effect on the amounts recognized in surplus or deficit. A one percentage point change in assumed healthcare cost trend rates would have the following effects:

	One percentage point increase	One percentage point deerease
Effect the aggregate of theservice cost intered cost	190	(150)
Effect on defined benefit obligation	1,000	(900)

Amounts for the current and previous four periods are as follows:
Defined benefit pension plans

	20x8	20x7	20x6	20x5	20x4
Defined benefit obligation	(23,300)	(18,400)	(11,600)	(10,582)	(9,144)
Plan assets	18,420	17,282	9,200	8,502	10,000
Surplus (deficit)	(3,880)	(1,120)	(2,400)	(2,080)	856
Experience adjustments on plan liabilities	(1,111)	(768)	(69)	543	(642)
Experience adjustments on plan assets	(300)	1,600	(1,078)	(2,890)	2,777

Post-employment medical benefits

	20x8	20x7	20x6	20x5	20x4
Defined benefit obligation	7,337	6,405	5,439	4,923	4,221
Experience adjustments on plan liabilities	(232)	829	490	(174)	(103)

The reporting entity also participates in a defined benefit plan for all local government units in Jurisdiction Y that provides pensions linked to final salaries and is funded on a pay-as-you-go basis. It is not practicable to determine the present value of the economic entity's obligation or the related current service cost, as the plan computes its obligations on a basis that differs materially from the basis used in [name of reporting entity]'s financial statements. [describe basis] On that basis, the plan's financial statements to June 30 20X6 show an unfunded liability of 27,525. The unfunded liability will result in future payments by participating employers. The plan has approximately 75,000 members, of whom approximately 5,000 are current or former employees of [name of reporting entity] or their dependants. The expense recognized in the statement of financial performance, which is equal to contributions due for the year, and is not included in the above amounts, was 230 (20X7: 215). The reporting entity's future contributions may be increased substantially if other entities withdraw from the plan.

Illustration of the Application of Paragraph 70

The Issue

IE8. Paragraph 69 of this Standard imposes a ceiling on the defined benefit asset that can be recognized.

> 69. **The amount determined under paragraph 65 may be negative (an asset). An entity shall measure the resulting asset at the lower of:**
>
> (a) **The amount determined under paragraph 65** [i.e., the surplus/deficit in the plan plus (minus) any unrecognized losses (gains)]; **and**
>
> (b) **The total of:**
>
> (i) **Any cumulative unrecognized net actuarial losses and past service cost (see paragraphs 105, 106 and 112); and**
>
> **(ii) The present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan. The present value of these economic benefits shall be determined using the discount rate specified in paragraph 91.**

IE9. Without paragraph 70 (see below), paragraph 69(b)(i) has the following consequence: sometimes deferring the recognition of an actuarial loss (gain) in determining the amount specified by paragraph 65 leads to a gain (loss) being recognized in the statement of financial performance.

IE10. The following example illustrates the effect of applying paragraph 69 without paragraph 70. The example assumes that the entity's accounting policy is not to recognize actuarial gains and losses within the corridor, and to amortize actuarial gains and losses outside the corridor. (Whether the corridor is used is not significant. The issue can arise whenever there is deferred recognition under paragraph 65.)

Example 1—Effect of applying paragraph 69 without paragraph 70

	A	**B**	**C**	**D=A+C**	**E=B+C**	**F=Lower of D and E**	**G**
Year	Surplus in plan	Economic benefits available (paragraph 69(b)(ii))	Losses un-recognized under paragraph 65	Paragraph 65	Paragraph 69(b)	Asset ceil-ing, i.e., recognized asset	Gain recognized in year 2
1	100	0	0	100	0	0	–
2	70	0	30	100	30	30	30

IE11. At the end of year 1, there is a surplus of 100 in the plan (column A in the table above), but no economic benefits are available to the entity either from refunds or reductions in future contributions* (column B). There are no unrecognized gains and losses under paragraph 65 (column C). So, if there were no asset ceiling, an asset of 100 would be recognized, being the amount specified by paragraph 65 (column D). The asset ceiling in paragraph 69 restricts the asset to nil (column F).

IE12. In year 2, there is an actuarial loss in the plan of 30 that reduces the surplus from 100 to 70 (column A), the recognition of which is deferred under paragraph 65 (column C). So, if there were no asset ceiling, an asset of 100 (column D) would be recognized. The asset ceiling without paragraph 70 would be 30 (column E). An asset of 30 would be recognized (column F), giving rise to an increase in revenue (column G), even though all that has happened is that a surplus from which the entity cannot benefit has decreased.

IE13. A similarly counter intuitive effect could arise with actuarial gains (to the extent that they reduce cumulative unrecognized actuarial losses).

Paragraph 70

IE14. Paragraph 70 prohibits the recognition of gains (losses) that arise solely from past service cost and actuarial losses (gains).

70. **The application of paragraph 69 shall not result in a gain being recognized solely as a result of an actuarial loss or past service cost in the current period, or in a loss being recognized solely as a result of an actuarial gain in the current period. The entity shall therefore recognize immediately under paragraph 65 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 69(b):**

* Based on the current terms of the plan.

(a) **Net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 69(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period shall be recognized immediately under paragraph 65.**

(b) **Net actuarial gains of the current period after the deduction of past service cost of the current period to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 69(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period shall be recognized immediately under paragraph 65.**

IE15. The following examples illustrate the result of applying paragraph 70. As above, it is assumed that the entity's accounting policy is not to recognize actuarial gains and losses within the corridor, and to amortize actuarial gains and losses outside the corridor. For the sake of simplicity, the periodic amortization of unrecognized gains and losses outside the corridor is ignored in the examples**.**

Example 1 continued—Adjustment when there are actuarial losses and no change in the economic benefits available

	A	**B**	**C**	**D=A+C**	**E=B+C**	**F=Lower of D and E**	**G**
Year	Surplus in plan	Economic benefits available (paragraph 69(b)(ii))	Losses un-recognized under paragraph 65	Paragraph 65	Paragraph 69(b)	Asset ceiling, i.e., recognized asset	Gain re cognized in year 2
1	100	0	0	100	0	0	–
2	70	0	0	70	0	0	0

IE16. The facts are as in example 1 above. Applying paragraph 70, there is no change in the economic benefits available to the entity* so the entire actuarial loss of 30 is recognized immediately under paragraph 65 (column D). The asset ceiling remains at nil (column F) and no gain is recognized.

* The term "economic benefits available to the entity" is used to refer to those economic benefits that qualify for recognition under paragraph 69(b)(ii).

IE17 In effect, the actuarial loss of 30 is recognized immediately, but is offset by the reduction in the effect of the asset ceiling.

	Asset in Statement of Financial Position under paragraph 65 (column D above)	**Effect of the asset ceiling**	**Asset ceiling (column F above**
Year 1	100	(100)	0
Year 2	70	(70)	0
Gain (loss)	(30)	(30)	0

IE18. In the above example, there is no change in the present value of the economic benefits available to the entity. The application of paragraph 70 becomes more complex when there are changes in present value of the economic benefits available, as illustrated in the following examples.

Example 2—Adjustment when there are actuarial losses and a decrease in the economic benefits available

	A	**B**	**C**	**D=A+C**	**E=B+C**	**F=lower of D and E**	**G**
Year	Surplus in plan	Economic benefits available (paragraph 69(b)(ii))	Losses un recognized under paragraph 65	Paragraph 65	Paragraph 69(b)	Asset ceiling,i.e., recognized asset	Gain recognized in year 2
1	60	30	40	100	70	70	–
2	25	20	50	75	70	70	0

IE19. At the end of year 1, there is a surplus of 60 in the plan (column A) and economic benefits available to the entity of 30 (column B). There are unrecognized losses of 40 under paragraph 65 (column C). So, if there were no asset ceiling, an asset of 100 would be recognized (column D). The asset ceiling restricts the asset to 70 (column F).

IE20. In year 2, an actuarial loss of 35 in the plan reduces the surplus from 60 to 25 (column A). The economic benefits available to the entity fall by 10 from 30 to 20 (column B). Applying paragraph 70, the actuarial loss of 35 is analyzed as follows:

Actuarial loss equal to the reduction in economic benefits	10
Actuarial loss that exceeds the reduction in economic benefits	25

IE21. In accordance with paragraph 70, 25 of the actuarial loss is recognized immediately under paragraph 65* (column D). The reduction in economic benefits of 10 is included in the cumulative unrecognized losses that increase to 50 (column C). The asset ceiling, therefore, also remains at 70 (column E) and no gain is recognized.

IE22. In effect, an actuarial loss of 25 is recognized immediately, but is offset by the reduction in the effect of the asset ceiling.

	Asset in Statement of Financial Position under paragraph 65 (column D above)	**Effect of the asset ceiling**	**Asset ceiling (column F above)**
Year 1	100	(30)	70
Year 2	75	(5)	70
Gain (loss)	(25)	25	0

Example 3—Adjustment when there are actuarial gains and a decrease in the economic benefits available to the entity

	A	**B**	**C**	**D=A+C**	**E=B+C**	**F=lower of D and E**	**G**
Year	Surplus in plan	Economic benefits available (paragraph 69(b)(ii))	Losses un-recognized under paragraph 65	Paragraph 65	Paragraph 69(b)	Asset ceil-ing, i.e., recognized asset	Gain recognized in year 2
1	60	30	40	100	70	70	–
2	110	25	40	150	65	65	(5)

IE23. At the end of year 1, there is a surplus of 60 in the plan (column A) and economic benefits available to the entity of 30 (column B). There are unrecognized losses of 40 under paragraph 65 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognized (column D). The asset ceiling restricts the asset to 70 (column F).

IE24. In year 2, an actuarial gain of 50 in the plan increases the surplus from 60 to 110 (column A). The economic benefits available to the entity decrease by 5

* The application of paragraph 70 allows the recognition of some actuarial gains and losses to be deferred under paragraph 65 and, hence, to be included in the calculation of the asset ceiling. For example, cumulative unrecognized actuarial losses that have built up while the amount specified by paragraph 69(b) is not lower than the amount specified by paragraph 65 will not be recognized immediately at the point that the amount specified by paragraph 69(b) becomes lower. Instead, their recognition will continue to be deferred in line with the entity's accounting policy. The cumulative unrecognized losses in this example are losses the recognition of which is deferred even though paragraph 70 applies.

(column B). Applying paragraph 70, there is no increase in economic benefits available to the entity. Therefore, the entire actuarial gain of 50 is recognized immediately under paragraph 65 (column D) and the cumulative unrecognized loss under paragraph 65 remains at 40 (column C). The asset ceiling decreases to 65 because of the reduction in economic benefits. That reduction is not an actuarial loss as defined by SLPSAS 19 and therefore does not qualify for deferred recognition.

IE25. In effect, an actuarial gain of 50 is recognized immediately, but is (more than) offset by the increase in the effect of the asset ceiling.

	Asset in Statement of Financial Position under paragraph 65 (column D above)	**Effect of the asset ceiling**	**Asset ceiling (column F above)**
Year 1	100	(30)	70
Year 2	150	(85)	65
Gain (loss)	50	(55)	(5)

IE26. In both examples 2 and 3, there is a reduction in economic benefits available to the entity. However, in example 2 no loss is recognized whereas, in example 3, a loss is recognized. This difference in treatment is consistent with the treatment of changes in the present value of economic benefits before application of paragraph 70. The purpose of paragraph 70 is solely to prevent gains (losses) being recognized because of past service cost or actuarial losses (gains). As far as is possible, all other consequences of deferred recognition and the asset ceiling are left unchanged.

Example 4—Adjustment in a period in which the asset ceiling ceases to have an effect

	A	**B**	**C**	**D=A+C**	**E=B+C**	**F=lower of D ans E**	**G**
Year	Surplus in plan	Economic benefits available (paragraph 69(b)(ii))	paragraph Losses un-recognized under 65	Paragraph 65	Paragraph 69(b)	Asset ceiling, i.e., recognized asset	Gain recognized in year 2
1	60	25	40	100	65	65	–
2	(50)	0	115	65	115	65	0

IE27. At the end of year 1, there is a surplus of 60 in the plan (column A) and economic benefits are available to the entity of 25 (column B). There are unrecognized losses of 40 under paragraph 65 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognized (column D). The asset ceiling restricts the asset to 65 (column F).

IE28. In year 2, an actuarial loss of 110 in the plan reduces the surplus from 60 to a deficit of 50 (column A). The economic benefits available to the entity decrease from 25 to 0 (column B). To apply paragraph 70, it is necessary to determine how much of the actuarial loss arises while the defined benefit asset is determined in accordance with paragraph 69(b). Once the surplus becomes a deficit, the amount determined by paragraph 65 is lower than the net total under paragraph 69(b). So, the actuarial loss that arises while the defined benefit asset is determined in accordance with paragraph 69(b) is the loss that reduces the surplus to nil, i.e., 60. The actuarial loss is, therefore, analyzed as follows:

Actuarial loss that arises while the defined benefit asset is measured under paragraph 69(b):

Actuarial loss that equals the reduction in economic benefits	25
Actuarial loss that exceeds the reduction in economic benefits	35
	60
Actuarial loss that arises while the defined benefit asset is measured under paragraph 65	50
Total actuarial loss	110

IE29. In accordance with paragraph 70, 35 of the actuarial loss is recognized immediately under paragraph 65 (column D); 75 (25 plus 50) of the actuarial loss is included in the cumulative unrecognized losses, which increase to 115 (column C). The amount determined under paragraph 65 becomes 65 (column D), and under paragraph 69(b) becomes 115 (column E). The recognized asset is the lower of the two, i.e., 65 (column F), and no gain or loss is recognized (column G).

IE30. In effect, an actuarial loss of 35 is recognized immediately, but is offset by the reduction in the effect of the asset ceiling

	Asset in Statement of Financial Position under paragraph 65 (column D above)	**Effect of the asset ceiling**	**Asset ceiling (column F above**
Year 1	100	(35)	65
Year 2	65	0	65
Gain (loss)	(35)	35	0

Notes

1. In applying paragraph 70 in situations when there is an increase in the present value of the economic benefits available to the entity, it is important to remember that the present value of the economic benefits available cannot exceed the surplus in the plan.*

2. In practice, benefit improvements often result in a past service cost and an increase in expected future contributions, due to increased current service costs of future years. The increase in expected future contributions may increase the economic benefits available to the entity in the form of anticipated reductions in those future contributions. The prohibition against recognizing a gain solely as a result of past service cost in the current period does not prevent the recognition of a gain because of an increase in economic benefits. Similarly, a change in actuarial assumptions that causes an actuarial loss may also increase expected future contributions and, hence, the economic benefits available to the entity in the form of anticipated reductions in future contributions. Again, the prohibition against recognizing a gain solely as a result of an actuarial loss in the current period does not prevent the recognition of a gain because of an increase in economic benefits.

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* In the example illustrating paragraph 73 of SLPSAS 19, the present value of available future refunds in contributions could not exceed the surplus in the plan of 90.

SLPSAS – 20 – Intangible Assets

Acknowledgement

Intangible Assets (SLPSAS – 20) of the "Sri Lanka Public Sector Accounting Standards – Volume III" is based on the Hand Book of International Public Sector Accounting Pronouncement of the International Public Sector Accounting Standards Boards (IPSASB), publish by the International Federation of Accountants (IFAC) in June 2014 and is used with permission of IFAC.

SLPSAS 20 - INTANGIBLE ASSETS
CONTENTS

Sri Lanka Public Sector Accounting Standard 20, Intangible Assets, is set out in paragraphs 1–133. All the paragraphs have equal authority. SLPSAS 20 should be read in the context of its objective and the Preface to Sri Lanka Public Sector Accounting Standards. SLPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors, provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognize an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets, and requires specified disclosures about intangible assets.

Scope

2. **An entity that prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for intangible assets.**

3. **This Standard shall be applied in accounting for intangible assets, except:**

   (a) **Intangible assets that are within the scope of another Standard;**

   (b) **Financial assets (see the relevant Sri Lanka Accounting Standard dealing with financial instruments);**

   (c) **The recognition and measurement of exploration and evaluation assets (see the relevant Sri Lanka Accounting Standard dealing with exploration for, and evaluation of, mineral resources);**

   (d) **Expenditure on the development and extraction of minerals, oil, natural gas and similar non-regenerative resources;**

   (e) **Intangible assets acquired in a business combination (see the relevant Sri Lanka Accounting Standard dealing with business combinations);**

   (f) **Goodwill acquired in a business combination (see the relevant Sri Lanka Accounting Standard dealing with business combinations);**

   (g) **Powers and rights conferred by legislation, a constitution, or by equivalent means;**

   (h) **Deferred tax assets (see the relevant Sri Lanka Accounting Standard dealing with income taxes);**

   (i) **Deferred acquisition costs, and intangible assets, arising from an insurer's contractual rights under insurance contracts within the scope of the relevant Sri Lanka Accounting Standard dealing with insurance contracts. In cases where the relevant Sri Lanka Accounting Standard does not set out specific disclosure requirements for those intangible assets, the disclosure requirements in this Standard apply to those intangible assets;**

(j) **Non-current intangible assets classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations; and**

(k) **In respect of intangible heritage assets. However, the disclosure requirements of paragraphs 115–127 apply to those heritage assets that are recognized.**

4. **This Standard applies to all public sector entities other than Government Business Enterprises.**

5. *The Preface to Sri Lanka Public Sector Accounting Standards* issued by the Public Sector Accounting Standards Committee of the Institute of Chartered Accountants of Sri Lanka (PSASC) explains that Government Business Enterprises (GBEs) apply IFRSs issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka). GBEs are defined in SLPSAS 1, *Presentation of Financial Statements.*

6. If another SLPSAS prescribes the accounting for a specific type of intangible asset, an entity applies that SLPSAS instead of this Standard. For example, this Standard does not apply to:

   (a) Intangible assets held by an entity for sale in the ordinary course of operations (see SLPSAS 16, *Construction Contracts, and SLPSAS 9, Inventories);*

   (b) Leases that are within the scope of SLPSAS 12, Leases; and

   (c) Assets arising from employee benefits *(see SLPSAS 19, Employee Benefits);*

7. Some intangible assets may be contained in or on a physical substance such as a compact disc (in the case of computer software), legal documentation (in the case of a licence or patent), or film. In determining whether an asset that incorporates both intangible and tangible elements should be treated under SLPSAS 7, Property, Plant, and Equipment, or as an intangible asset under this Standard, an entity uses judgement to assess which element is more significant. For example, the navigation software for a fighter aircraft is integral to the aircraft and is treated as property, plant and equipment. The same applies to the operating system of a computer. When the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

8. This Standard applies to, among other things, expenditure on advertising, training, start-up, research, and development activities. Research and development activities are directed to the development of knowledge. Therefore, although these activities may result in an asset with physical substance (e.g., a prototype), the physical element of the asset is secondary to its intangible component, i.e., the knowledge embodied in it.

9. In the case of a finance lease, the underlying asset may be either tangible or intangible. After initial recognition, a lessee accounts for an intangible asset held under a finance lease in accordance with this Standard. Rights under licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents, and copyrights are excluded from the scope of SLPSAS 12 and are within the scope of this Standard.

10. Exclusions from the scope of a Standard may occur if activities or transactions are so specialized that they give rise to accounting issues that may need to be dealt with in a different way. Such issues arise in the accounting for expenditure on the exploration for, or development and extraction of, oil, gas, and mineral deposits in extractive industries, and in the case of insurance contracts. Therefore, this Standard does not apply to expenditure on such activities and contracts. However, this Standard applies to other intangible assets used (such as computer software), and other expenditure incurred (such as start-up costs), in extractive industries, or by insurers.

Intangible Heritage Assets

11. This Standard does not require an entity to recognize intangible heritage assets that would otherwise meet the definition of, and recognition criteria for, intangible assets. If an entity does recognize intangible heritage assets, it must apply the disclosure requirements of this Standard and may, but is not required to, apply the measurement requirements of this Standard.

12. Some intangible assets are described as intangible heritage assets because of their cultural, environmental, or historical significance. Examples of intangible heritage assets include recordings of significant historical events and rights to use the likeness of a significant public person on, for example, postage stamps or collectible coins. Certain characteristics, including the following, are often displayed by intangible heritage assets (although these characteristics are not exclusive to such assets):

    (a) Their value in cultural, environmental, and historical terms is unlikely to be fully reflected in a financial value based purely on a market price;

    (b) Legal and/or statutory obligations may impose prohibitions or severe restrictions on disposal by sale;

    (c) Their value may increase over time; and

    (d) It may be difficult to estimate their useful lives, which in some cases could be several hundred years.

13. Public sector entities may have large holdings of intangible heritage assets that have been acquired over many years and by various means, including purchase, donation, bequest, and sequestration. These assets are rarely held for their ability to generate cash inflows, and there may be legal or social obstacles to using them for such purposes.

14. Some intangible heritage assets have future economic benefits or service potential other than their heritage value, for example, royalties paid to the entity for use of an historical recording. In these cases, an intangible heritage asset may be recognized and measured on the same basis as other items of cash-generating intangible assets. For other intangible heritage assets, their future economic benefit or service potential is limited to their heritage characteristics. The existence of both future economic benefits and service potential can affect the choice of measurement base.

15. The disclosure requirements in paragraphs 117–124 require entities to make disclosures about recognized intangible assets. Therefore, entities that recognize intangible heritage assets are required to disclose in respect of those assets such matters as, for example:

    (a) The measurement basis used;

    (b) The amortization method used, if any;

    (c) The gross carrying amount;

    (d) The accumulated amortization at the end of the period, if any; and

    (e) A reconciliation of the carrying amount at the beginning and end of the period showing certain components thereof.

Definitions

16. **The following terms are used in this Standard with the meanings specified:**

    Amortization is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

    Carrying amount is the amount at which an asset is recognized after deducting any accumulated amortization and accumulated impairment losses.

    Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.

    An intangible asset is an identifiable non monetary asset without physical substance.

    Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

    Terms defined in other SLPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the Glossary of *Defined Terms published separately.*

Intangible Assets

17. Entities frequently expend resources, or incur liabilities, on the acquisition, development, maintenance, or enhancement of intangible resources such as scientific or technical knowledge, design and implementation of new processes, or systems, licences, intellectual property, and trademarks (including brand names and publishing titles). Common examples of items encompassed by these broad headings are computer software, patents, copyrights, motion picture films, lists of users of a service, acquired fishing licences, acquired import quotas, and relationships with users of a service.

18. Not all the items described in paragraph 17 meet the definition of an intangible asset, i.e., identifiability, control over a resource, and existence of future economic benefits or service potential. If an item within the scope of this Standard does not meet the definition of an intangible asset, expenditure to acquire it or generate it internally is recognized as an expense when it is incurred.

19. **An asset is identifiable if it either:**

    (a) **Is separable, i.e., is capable of being separated or divided from the entity and sold, transferred, licensed, rented, or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or**

    (b) **Arises from binding arrangements (including rights from contracts or other legal rights), regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.**

20. For the purposes of this Standard, a binding arrangement describes an arrangement that confers similar rights and obligations on the parties to it as if it were in the form of a contract.

Control of an Asset

21. An entity controls an asset if the entity has the power to obtain the future economic benefits or service potential flowing from the underlying resource and to restrict the access of others to those benefits or that service potential. The capacity of an entity to control the future economic benefits or service potential from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits or service potential in some other way.

22. Scientific or technical knowledge may give rise to future economic benefits or service potential. An entity controls those benefits or that service potential if, for example, the knowledge is protected by legal rights

such as copyrights, a restraint of trade agreement (where permitted), or by a legal duty on employees to maintain confidentiality.

23. An entity may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits or service potential from training. The entity may also expect that the staff will continue to make their skills available to the entity. However, an entity usually has insufficient control over the expected future economic benefits or service potential arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits or service potential expected from it, and it also meets the other parts of the definition.

24. An entity may have a portfolio of users of its services or its success rate in reaching intended users of its services and expect that, because of its efforts in building relationships with users of its services, those users will continue to use its services. However, in the absence of legal rights to protect, or other ways to control the relationships with users of a service or the loyalty of those users, the entity usually has insufficient control over the expected economic benefits or service potential from relationships with users of a service and loyalty for such items (e.g., portfolio of users of a service, market shares or success rates of a service, relationships with, and loyalty of, users of a service) to meet the definition of intangible assets. In the absence of legal rights to protect such relationships, exchange transactions for the same or similar non-contractual customer relationships provide evidence that the entity is nonetheless able to control the expected future economic benefits or service potential flowing from the relationships with the users of a service. Because such exchange transactions also provide evidence that the relationships with users of a service are separable, those relationships meet the definition of an intangible asset.

Future Economic Benefits or Service Potential

25. The future economic benefits or service potential flowing from an intangible asset may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity. For example, the use of intellectual property in a production or service process may reduce future production or service costs or improve service delivery rather than increase future revenues (e.g., an on-line system that allows citizens to renew driving licences more quickly on-line, resulting in a reduction in office staff required to perform this function while increasing the speed of processing).

Recognition and Measurement

26. The recognition of an item as an intangible asset requires an entity to demonstrate that the item meets:

(a) The definition of an intangible asset (see paragraphs 17–25); and

(b) The recognition criteria (see paragraphs 28–30).

This requirement applies to the cost measured at recognition (the cost in an exchange transaction or to internally generate an intangible asset, or the fair value of an intangible asset acquired through a non-exchange transaction) and those incurred subsequently to add to, replace part of, or service it.

27. The nature of intangible assets is such that, in many cases, there are no additions to such an asset or replacements of part of it. Accordingly, most subsequent expenditures are likely to maintain the expected future economic benefits or service potential embodied in an existing intangible asset rather than meet the definition of an intangible asset and the recognition criteria in this Standard. In addition, it is often difficult to attribute subsequent expenditure directly to a particular intangible asset rather than to the entity's operations as a whole. Therefore, only rarely will subsequent expenditure—expenditure incurred after the initial recognition of an acquired intangible asset or after completion of an internally generated intangible asset—be recognized in the carrying amount of an asset. Consistent with paragraph 61, subsequent expenditure on brands, mastheads, publishing titles, lists users of a service, and items similar in substance (whether externally acquired or internally generated) is always recognized in surplus or deficit as incurred. This is because such expenditure cannot be distinguished from expenditure to develop the entity's operations as a whole.

28. **An intangible asset shall be recognized if, and only if:**

(a) **It is probable that the expected future economic benefits or service potential that are attributable to the asset will flow to the entity; and**

(b) **The cost or fair value of the asset can be measured reliably.**

29. **An entity shall assess the probability of expected future economic benefits or service potential using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset.**

30. An entity uses judgement to assess the degree of certainty attached to the flow of future economic benefits or service potential that are attributable to the use of the asset on the basis of the evidence available at the time of initial recognition, giving greater weight to external evidence.

31. **An intangible asset shall be measured initially at cost in accordance with paragraphs 32–43. Where an intangible asset is acquired through a non-exchange transaction, its initial cost at the date of acquisition, shall be measured at its fair value as at that date.**

Separate Acquisition

32. Normally, the price an entity pays to acquire separately an intangible asset will reflect expectations about the probability that the expected future economic benefits or service potential embodied in the asset will flow to the entity. In other words, the entity expects there to be an inflow of economic benefits or service potential, even if there is uncertainty about the timing or the amount of the inflow. Therefore, the probability recognition criterion in paragraph 28(a) is always considered to be satisfied for separately acquired intangible assets.

33. In addition, the cost of a separately acquired intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.

34. The cost of a separately acquired intangible asset comprises:

    (a) Its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and

    (b) Any directly attributable cost of preparing the asset for its intended use.

35. Examples of directly attributable costs are:

    (a) Costs of employee benefits (as defined in SLPSAS 19) arising directly from bringing the asset to its working condition;

    (b) Professional fees arising directly from bringing the asset to its working condition; and

    (c) Costs of testing whether the asset is functioning properly.

36. Examples of expenditures that are not part of the cost of an intangible asset are:

    (a) Costs of introducing a new product or service (including costs of advertising and promotional activities);

    (b) Costs of conducting operations in a new location or with a new class of users of a service (including costs of staff training); and

    (c) Administration and other general overhead costs.

37. Recognition of costs in the carrying amount of an intangible asset ceases when the asset is in the condition necessary for it to be capable of operating in the manner intended by management. Therefore, costs incurred in using or redeploying an intangible asset are not included in the carrying amount of that asset. For example, the following costs are not included in the carrying amount of an intangible asset:

    (a) Costs incurred while an asset capable of operating in the manner intended by management has yet to be brought into use; and

(b) Initial operating deficits, such as those incurred while demand for the asset's output builds up.

38. Some operations occur in connection with the development of an intangible asset, but are not necessary to bring the asset to the condition necessary for it to be capable of operating in the manner intended by management. These incidental operations may occur before or during the development activities. Because incidental operations are not necessary to bring an asset to the condition necessary for it to be capable of operating in the manner intended by management, the revenue and related expenses of incidental operations are recognized immediately in surplus or deficit, and included in their respective classifications of revenue and expense.

39. If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. The difference between this amount and the total payments is recognized as interest expense over the period of credit unless it is capitalized in accordance with the capitalization treatment permitted in SLPSAS 4, Borrowing Costs.

Subsequent Expenditure on an Acquired In-process Research and Development Project

40. **Research or development expenditure that:**

(a) **Relates to an in-process research or development project acquired separately and recognized as an intangible asset; and**

(b) **Is incurred after the acquisition of that project;**

shall be accounted for in accordance with paragraphs 52–60.

41. Applying the requirements in paragraphs 52–60 means that subsequent expenditure on an in-process research or development project acquired separately and recognized as an intangible asset is:

(a) Recognized as an expense when incurred if it is research expenditure;

(b) Recognized as an expense when incurred if it is development expenditure that does not satisfy the criteria for recognition as an intangible asset in paragraph 55; and

(c) Added to the carrying amount of the acquired in-process research or development project if it is development expenditure that satisfies the recognition criteria in paragraph 55.

Intangible Assets Acquired through Non-Exchange Transactions

42. In some cases, an intangible asset may be acquired through a non-exchange transaction. This may happen when another public sector entity transfers to an entity in a non-exchange transaction, intangible assets such as airport landing rights, licences to operate radio or television stations,

import licences or quotas or rights to access other restricted resources. A private citizen, for example a Nobel Prize winner, may bequeath his or her personal papers, including the copyright to his or her publications to the national archives (a public sector entity) in a non-exchange transaction.

43. Under these circumstances the cost of the item is its fair value at the date it is acquired. For the purposes of this Standard, the measurement at recognition of an intangible asset acquired through a non-exchange transaction, at its fair value consistent with the requirements of paragraph 74, does not constitute a revaluation. Accordingly, the revaluation requirements in paragraph 74, and the supporting commentary in paragraphs 75–86 only apply when an entity elects to revalue an intangible item in subsequent reporting periods.

Exchanges of Assets

44. One or more intangible assets may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The following discussion refers simply to an exchange of one non-monetary asset for another, but it also applies to all exchanges described in the preceding sentence. The cost of such an intangible asset is measured at fair value unless the fair value of neither the asset received nor the asset given up is reliably measurable. The acquired asset is measured in this way even if an entity cannot immediately derecognize the asset given up. If the acquired asset is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

45. Paragraph 28(b) specifies that a condition for the recognition of an intangible asset is that the cost of the asset can be measured reliably. The fair value of an intangible asset for which comparable market transactions do not exist is reliably measurable if:

    (a) The variability in the range of reasonable fair value estimates is not significant for that asset: or

    (b) The probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value.

    If an entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

Internally Generated Goodwill

46. **Internally generated goodwill shall not be recognized as an asset.**

47. In some cases, expenditure is incurred to generate future economic benefits or service potential, but it does not result in the creation of an intangible asset that meets the recognition criteria in this Standard. Such expenditure is often described as contributing to internally generated

goodwill. Internally generated goodwill is not recognized as an asset because it is not an identifiable resource (i.e., it is not separable nor does it arise from binding arrangements (including rights from contracts or other legal rights) controlled by the entity that can be measured reliably at cost.

48. Differences between the market value of an entity and the carrying amount of its identifiable net assets at any time may capture a range of factors that affect the value of the entity. However, such differences do not represent the cost of intangible assets controlled by the entity.

Internally Generated Intangible Assets

49. It is sometimes difficult to assess whether an internally generated intangible asset qualifies for recognition because of problems in:

(a) Identifying whether and when there is an identifiable asset that will generate expected future economic benefits or service potential; and

(b) Determining the cost of the asset reliably. In some cases, the cost of generating an intangible asset internally cannot be distinguished from the cost of maintaining or enhancing the entity's internally generated goodwill or of running day-to-day operations.

Therefore, in addition to complying with the general requirements for the recognition and initial measurement of an intangible asset, an entity applies the requirements and guidance in paragraphs 50–65 to all internally generated intangible assets.

50. To assess whether an internally generated intangible asset meets the criteria for recognition, an entity classifies the generation of the asset into:

(a) A research phase; and

(b) A development phase.

Although the terms "research" and "development" are defined, the terms "research phase" and "development phase" have a broader meaning for the purpose of this Standard.

51. If an entity cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the entity treats the expenditure on that project as if it were incurred in the research phase only.

Research Phase

52. **No intangible asset arising from research (or from the research phase of an internal project) shall be recognized. Expenditure on research (or on the research phase of an internal project) shall be recognized as an expense when it is incurred.**

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

54. Examples of research activities are:

    (a) Activities aimed at obtaining new knowledge;

    (b) The search for, evaluation and final selection of, applications of research findings or other knowledge;

    (c) The search for alternatives for materials, devices, products, processes, systems, or services; and

    (d) The formulation, design, evaluation, and final selection of possible alternatives for new or improved materials, devices, products, processes, systems, or services.

Development Phase

55. **An intangible asset arising from development (or from the development phase of an internal project) shall be recognized if, and only if, an entity can demonstrate all of the following:**

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

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

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

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

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

    (f) **Its ability to measure reliably the expenditure attributable to the intangible asset during its development.**

56. In the development phase of an internal project, an entity can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits or service potential. This is because the development phase of a project is further advanced than the research phase.

57. Examples of development activities are:

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

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

(c) The design, construction, and operation of a pilot plant or operation that is not of a scale economically feasible for commercial production or use in providing services;

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

(e) Website costs and software development costs.

58. [Not used to maintain consistency of paragraph numbers with SLPSASs].

59. Availability of resources to complete, use, and obtain the benefits from an intangible asset can be demonstrated by, for example, an operating plan showing the technical, financial, and other resources needed and the entity's ability to secure those resources. In some cases, an entity demonstrates the availability of external finance by obtaining a lender's or funder's indication of its willingness to fund the plan.

60. An entity's costing systems can often measure reliably the cost of generating an intangible asset internally, such as salary and other expenditure incurred in securing logos, copyrights or licences, or developing computer software.

61. **Internally generated brands, mastheads, publishing titles, lists of users of a service, and items similar in substance shall not be recognized as intangible assets.**

62. Expenditure on internally generated brands, mastheads, publishing titles, lists of users of a service, and items similar in substance cannot be distinguished from the cost of developing the entity's operations as a whole. Therefore, such items are not recognized as intangible assets.

Cost of an Internally Generated Intangible Asset

63. The cost of an internally generated intangible asset for the purpose of paragraph 31 is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria in paragraphs 28, 29, and 55. Paragraph 70 prohibits reinstatement of expenditure previously recognized as an expense.

64. The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce, and prepare the asset to be capable of operating in the manner intended by management. Examples of directly attributable costs are:

(a) Costs of materials and services used or consumed in generating the intangible asset;

(b) Costs of employee benefits (as defined in SLPSAS 19) arising from the generation of the intangible asset;

(c) Fees to register a legal right; and

(d) Amortization of patents and licences that are used to generate the intangible asset.

SLPSAS 4 specifies criteria for the recognition of interest as an element of the cost of an asset that is a qualifying asset.

65. The following are not components of the cost of an internally generated intangible asset:

(a) Selling, administrative and other general overhead expenditure unless this expenditure can be directly attributed to preparing the asset for use;

(b) Identified inefficiencies and initial operating deficits incurred before the asset achieves planned performance; and

(c) Expenditure on training staff to operate the asset.

Recognition of an Expense

66. **Expenditure on an intangible item shall be recognized as an expense when it is incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria (see paragraphs 26–65).**

67. In some cases, expenditure is incurred to provide future economic benefits or service potential to an entity, but no intangible asset or other asset is acquired or created that can be recognized. In the case of the supply of goods, the entity recognizes such expenditure as an expense when it has a right to access those goods. In the case of the supply of services, the entity recognizes the expenditure as an expense when it receives the services. For example, expenditure on research is recognized as an expense when it is incurred (see paragraph 52). Other examples of expenditure that is recognized as an expense when it is incurred include:

(a) Expenditure on start-up activities (i.e., start-up costs), unless this expenditure is included in the cost of an item of property, plant, and equipment in accordance with SLPSAS 7. Start-up costs may consist of establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or operation (i.e., pre-opening costs), or expenditures for starting new operations or launching new products or processes (i.e., pre-operating costs);

(b) Expenditure on training activities;

(c) Expenditure on advertising and promotional activities (including mail order catalogues and information pamphlets); and

(d) Expenditure on relocating or reorganizing part or all of an entity.

68. An entity has a right to access goods when it owns them. Similarly, it has a right to access goods when they have been constructed by a supplier in accordance with the terms of a supply contract and the entity could demand delivery of them in return for payment. Services are received when they are performed by a supplier in accordance with a contract to deliver them to the entity and not when the entity uses them to deliver another service, for example, to deliver information about a service to users of that service.

69. Paragraph 66 does not preclude an entity from recognizing a prepayment as an asset when payment for goods has been made in advance of the entity obtaining a right to access those goods. Similarly, paragraph 66 does not preclude an entity from recognizing a prepayment as an asset when payment for services has been made in advance of the entity receiving those services.

Past Expenses not to be Recognized as an Asset

70. Expenditure on an intangible item that was initially recognized as an expense under this Standard shall not be recognized as part of the cost of an intangible asset at a later date.

Subsequent Measurement

71. An entity shall choose either the cost model in paragraph 73 or the revaluation model in paragraph 74 as its accounting policy. If an intangible asset is accounted for using the revaluation model, all the other assets in its class shall also be accounted for using the same model, unless there is no active market for those assets.

72. A class of intangible assets is a grouping of assets of a similar nature and use in an entity's operations. The items within a class of intangible assets are revalued simultaneously to avoid selective revaluation of assets and the reporting of amounts in the financial statements representing a mixture of costs and values as at different dates.

Cost Model

73. **After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortization and any accumulated impairment losses.**

Revaluation Model

74. **After initial recognition, an intangible asset shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated amortization. For the purpose of revaluations under this Standard, fair value shall be determined by reference to an**

active market. Revaluations shall be made with such regularity that at the reporting date the carrying amount of the asset does not differ materially from its fair value.

75. The revaluation model does not allow:

 (a) The revaluation of intangible assets that have not previously been recognized as assets; or

 (b) The initial recognition of intangible assets at amounts other than cost.

76. The revaluation model is applied after an asset has been initially recognized at cost. However, if only part of the cost of an intangible asset is recognized as an asset because the asset did not meet the criteria for recognition until part of the way through the process (see paragraph 63), the revaluation model may be applied to the whole of that asset. Also, the revaluation model may be applied to an intangible asset that was received through a non-exchange transaction (see paragraphs 42–43).

77. It is uncommon for an active market to exist for an intangible asset, although this may happen. For example, in some jurisdictions, an active market may exist for freely transferable homogeneous classes of licences or production quotas the entity has acquired from another entity. However, an active market cannot exist for brands, newspaper mastheads, music and film publishing rights, patents, or trademarks, because each such asset is unique. Also, although intangible assets are bought and sold, contracts are negotiated between individual buyers and sellers, and transactions are relatively infrequent. For these reasons, the price paid for one asset may not provide sufficient evidence of the fair value of another. Moreover, prices are often not available to the public.

78. The frequency of revaluations depends on the volatility of the fair values of the intangible assets being revalued. If the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is necessary. Some intangible assets may experience significant and volatile movements in fair value, thus necessitating annual revaluation. Such frequent revaluations are unnecessary for intangible assets with only insignificant movements in fair value.

79. If an intangible asset is revalued, any accumulated amortization at the date of the revaluation is either:

 (a) Restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount; or

 (b) Eliminated against the gross carrying amount of the asset and the net amount restated to the revalued amount of the asset.

80. **If an intangible asset in a class of revalued intangible assets cannot be revalued because there is no active market for this asset, the asset shall be carried at its cost less any accumulated amortization and impairment losses.**

81. **If the fair value of a revalued intangible asset can no longer be determined by reference to an active market, the carrying amount of the asset shall be its revalued amount at the date of the last revaluation by reference to the active market less any subsequent accumulated amortization and any subsequent accumulated impairment losses.**

82. The fact that an active market no longer exists for a revalued intangible asset may indicate that the asset may be impaired.

83. If the fair value of the asset can be determined by reference to an active market at a subsequent measurement date, the revaluation model is applied from that date.

84. **If an intangible asset's carrying amount is increased as a result of a revaluation, the increase shall be credited directly to revaluation surplus. However, the increase shall be recognized in surplus or deficit to the extent that it reverses a revaluation decrease of the same asset previously recognized in surplus or deficit.**

85. **If an intangible asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognized in surplus or deficit. However, the decrease shall be recognized directly in net assets/equity to the extent of any credit balance in the revaluation surplus in respect of that asset. The decrease recognized directly in net assets/equity reduces the amount accumulated in net assets/equity under the heading of revaluation surplus.**

86. The cumulative revaluation surplus included in net assets/equity may be transferred directly to accumulated surpluses or deficits when the surplus is realized. The whole surplus may be realized on the retirement or disposal of the asset. However, some of the surplus may be realized as the asset is used by the entity; in such a case, the amount of the surplus realized is the difference between amortization based on the revalued carrying amount of the asset and amortization that would have been recognized based on the asset's historical cost. The transfer from revaluation surplus to accumulated surpluses or deficits is not made through surplus or deficit.

Useful Life

87. **An entity shall assess whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that useful life. An intangible asset shall be regarded by the entity as having an indefinite useful life when, based**

on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for, or provide service potential to, the entity.

88. The accounting for an intangible asset is based on its useful life. An intangible asset with a finite useful life is amortized (see paragraphs 96–105), and an intangible asset with an indefinite useful life is not (see paragraphs 106–109). The Illustrative Examples accompanying this Standard illustrate the determination of useful life for different intangible assets, and the subsequent accounting for those assets based on the useful life determinations.

89. Many factors are considered in determining the useful life of an intangible asset, including:

(a) The expected usage of the asset by the entity and whether the asset could be managed efficiently by another management team;

(b) Typical product life cycles for the asset and public information on estimates of useful lives of similar assets that are used in a similar way;

(c) Technical, technological, commercial, or other types of obsolescence;

(d) The stability of the industry in which the asset operates and changes in the market demand for the products or services output from the asset;

(e) Expected actions by competitors or potential competitors;

(f) The level of maintenance expenditure required to obtain the expected future economic benefits or service potential from the asset and the entity's ability and intention to reach such a level;

(g) The period of control over the asset and legal or similar limits on the use of the asset, such as the expiry dates of related leases; and

(h) Whether the useful life of the asset is dependent on the useful life of other assets of the entity.

90. The term "indefinite" does not mean "infinite." The useful life of an intangible asset reflects only that level of future maintenance expenditure required to maintain the asset at its standard of performance assessed at the time of estimating the asset's useful life, and the entity's ability and intention to reach such a level. A conclusion that the useful life of an intangible asset is indefinite should not depend on planned future expenditure in excess of that required to maintain the asset at that standard of performance.

91. Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it is likely that their useful life is short.

92. The useful life of an intangible asset may be very long or even indefinite. Uncertainty justifies estimating the useful life of an intangible asset on a prudent basis, but it does not justify choosing a life that is unrealistically short.

93. **The useful life of an intangible asset that arises from binding arrangements (including rights from contracts or other legal rights) shall not exceed the period of the binding arrangement (including rights from contracts or other legal rights), but may be shorter depending on the period over which the entity expects to use the asset. If the binding arrangements (including rights from contracts or other legal rights) are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.**

94. There may be economic, political, social, and legal factors influencing the useful life of an intangible asset. Economic, political, or social factors determine the period over which future economic benefits or service potential will be received by the entity. Legal factors may restrict the period over which the entity controls access to such economic benefits or service potential. The useful life is the shorter of the periods determined by these factors.

95. Existence of the following factors, among others, indicates that an entity would be able to renew the binding arrangements (including rights from contracts or other legal rights) without significant cost:

   (a) There is evidence, possibly based on experience, that the binding arrangements (including rights from contracts or other legal rights) will be renewed. If renewal is contingent upon the consent of a third party, this includes evidence that the third party will give its consent;

   (b) There is evidence that any conditions necessary to obtain renewal will be satisfied; and

   (c) The cost to the entity of renewal is not significant when compared with the future economic benefits or service potential expected to flow to the entity from renewal.

   If the cost of renewal is significant when compared with the future economic benefits or service potential expected to flow to the entity from renewal, the “renewal” cost represents, in substance, the cost to acquire a new intangible asset at the renewal date.

Intangible Assets with Finite Useful Lives

Amortization Period and Amortization Method

96. **The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. Amortization shall begin when the asset is available for use, i.e., when**

it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortization shall cease at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations and the date that the asset is derecognized. The amortization method used shall reflect the pattern in which the asset's future economic benefits or service potential are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used. The amortization charge for each period shall be recognized in surplus or deficit unless this or another Standard permits or requires it to be included in the carrying amount of another asset.

97. A variety of amortization methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method, and the unit of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits or service potential embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits or service potential.

98. Amortization is usually recognized in surplus or deficit. However, sometimes the future economic benefits or service potential embodied in an asset are absorbed in producing other assets. In this case, the amortization charge constitutes part of the cost of the other asset and is included in its carrying amount. For example, the amortization of intangible assets used in a production process is included in the carrying amount of inventories (see SLPSAS 9).

Residual Value

99. **The residual value of an intangible asset with a finite useful life shall be assumed to be zero unless:**
    (a) **There is a commitment by a third party to acquire the asset at the end of its useful life; or**
    (b) **There is an active market for the asset, and:**
        (i) **Residual value can be determined by reference to that market; and**
        (ii) **It is probable that such a market will exist at the end of the asset's useful life.**

100. The depreciable amount of an asset with a finite useful life is determined after deducting its residual value. A residual value other than zero implies that an entity expects to dispose of the intangible asset before the end of its economic life.

101. An estimate of an asset's residual value is based on the amount recoverable from disposal using prices prevailing at the date of the estimate for the sale of a similar asset that has reached the end of its useful life and has operated under conditions similar to those in which the asset will be used. The residual value is reviewed at least at each reporting date. A change in the asset's residual value is accounted for as a change in an accounting estimate in accordance with SLPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors.*

102. The residual value of an intangible asset may increase to an amount equal to or greater than the asset's carrying amount. If it does, the asset's amortization charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount.

Review of Amortization Period and Amortization Method

103. **The amortization period and the amortization method for an intangible asset with a finite useful life shall be reviewed at least at each reporting date. If the expected useful life of the asset is different from previous estimates, the amortization period shall be changed accordingly. If there has been a change in the expected pattern of consumption of the future economic benefits or service potential embodied in the asset, the amortization method shall be changed to reflect the changed pattern. Such changes shall be accounted for as changes in accounting estimates in accordance with SLPSAS 3.**

104. During the life of an intangible asset, it may become apparent that the estimate of its useful life is inappropriate. For example, the recognition of an impairment loss may indicate that the amortization period needs to be changed.

105. Over time, the pattern of future economic benefits or service potential expected to flow to an entity from an intangible asset may change. For example, it may become apparent that a diminishing balance method of amortization is appropriate rather than a straight-line method. Another example is if use of the rights represented by a licence is deferred pending action on other components of the entity's strategic plan. In this case, economic benefits or service potential that flow from the asset may not be received until later periods.

Intangible Assets with Indefinite Useful Lives

106. **An intangible asset with an indefinite useful life shall not be amortized.**

107. An entity is required to test an intangible asset with an indefinite useful life or an intangible asset not yet available for use for impairment by comparing its recoverable service amount or its recoverable amount, as appropriate, with its carrying amount:

(a) Annually; and

(b) Whenever there is an indication that the intangible asset may be impaired.

Review of Useful Life Assessment

108. **The useful life of an intangible asset that is not being amortized shall be reviewed each reporting period to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite shall be accounted for as a change in an accounting estimate in accordance with SLPSAS 3.**

109. For intangible assets measured under the cost model, reassessing the useful life of an intangible asset as finite rather than indefinite is an indicator that the asset may be impaired.

Recoverability of the Carrying Amount—Impairment Losses

110. To determine whether an intangible asset measured under the cost model is impaired, and to determine the amount of such impairment, an entity adopts an accounting policy or accounting policies in accordance with SLPSAS 3.

Retirements and Disposals

111. **An intangible asset shall be derecognized:**

(a) **On disposal (including disposal through a non-exchange transaction); or**

(b) **When no future economic benefits or service potential are expected from its use or disposal.**

112. **The gain or loss arising from the derecognition of an intangible asset shall be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It shall be recognized in surplus or deficit when the asset is derecognized (unless SLPSAS 12 requires otherwise on a sale and leaseback).**

113. The disposal of an intangible asset may occur in a variety of ways (e.g., by sale, by entering into a finance lease, or through a non-exchange transaction). In determining the date of disposal of such an asset, an entity applies the criteria in SLPSAS 10, Revenue from Exchange Transactions for recognizing revenue from the sale of goods. SLPSAS 12 applies to disposal by a sale and leaseback.

114. If, in accordance with the recognition principle in paragraph 28, an entity recognizes in the carrying amount of an asset the cost of a replacement for part of an intangible asset, then it derecognizes the carrying amount of the replaced part. If it is not practicable for an entity to determine the carrying amount of the replaced part, it may use the cost of the replacement as

an indication of what the cost of the replaced part was at the time it was acquired or internally generated.

115. The consideration receivable on disposal of an intangible asset is recognized initially at its fair value. If payment for the intangible asset is deferred, the consideration received is recognized initially at the cash price equivalent. The difference between the nominal amount of the consideration and the cash price equivalent is recognized as interest revenue in accordance with SLPSAS 10 reflecting the effective yield on the receivable.

116. Amortization of an intangible asset with a finite useful life does not cease when the intangible asset is no longer used, unless the asset has been fully depreciated or is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations.

Disclosure

General

117. **An entity shall disclose the following for each class of intangible assets, distinguishing between internally generated intangible assets and other intangible assets:**

   (a) **Whether the useful lives are indefinite or finite and, if finite, the useful lives or the amortization rates used;**

   (b) **The amortization methods used for intangible assets with finite useful lives;**

   (c) **The gross carrying amount and any accumulated amortization (aggregated with accumulated impairment losses) at the beginning and end of the period;**

   (d) **The line item(s) of the statement of financial performance in which any amortization of intangible assets is included;**

   (e) **A reconciliation of the carrying amount at the beginning and end of the period showing:**

      (i) **Additions, indicating separately those from internal development and those acquired separately;**

      (ii) **Assets classified as held for sale or included in a disposal group classified as held for sale in accordance with the relevant Sri Lanka Accounting Standard dealing with non-current assets held for sale and discontinued operations and other disposals;**

      (iii) **Increases or decreases during the period resulting from revaluations under paragraphs 74, 84 and 85 (if any);**

(iv) **Impairment losses recognized in surplus or deficit during the period (if any);**

(v) **Impairment losses reversed in surplus or deficit during the period (if any);**

(vi) **Any amortization recognized during the period;**

(vii) **Net exchange differences arising on the translation of the financial statements into the presentation currency, and on the translation of a foreign operation into the presentation currency of the entity; and**

(viii) **Other changes in the carrying amount during the period.**

118. A class of intangible assets is a grouping of assets of a similar nature and use in an entity's operations. Examples of separate classes may include:

(a) Brand names;

(b) Mastheads and publishing titles;

(c) Computer software;

(d) Licences;

(e) Copyrights, patents, and other industrial property rights, service, and operating rights;

(f) Recipes, formulae, models, designs, and prototypes; and

(g) Intangible assets under development.

The classes mentioned above are disaggregated (aggregated) into smaller (larger) classes if this results in more relevant information for the users of the financial statements.

119. An entity discloses information on impaired intangible assets in addition to the information required by paragraph 117(e)(iii)–(v).

120. SLPSAS 3 requires an entity to disclose the nature and amount of a change in an accounting estimate that has a material effect in the current period or is expected to have a material effect in subsequent periods. Such disclosure may arise from changes in:

(a) The assessment of an intangible asset's useful life;

(b) The amortization method; or

(c) Residual values.

121. **An entity shall also disclose:**

(a) **For an intangible asset assessed as having an indefinite useful life, the carrying amount of that asset and the reasons supporting the assessment of an indefinite useful life. In giving these reasons, the**

entity shall describe the factor(s) that played a significant role in determining that the asset has an indefinite useful life.

(b) **A description, the carrying amount, and remaining amortization period of any individual intangible asset that is material to the entity's financial statements.**

(c) **For intangible assets acquired through a non-exchange transaction and initially recognized at fair value (see paragraphs 42–43):**

   (i) **The fair value initially recognized for these assets;**

   (ii) **Their carrying amount; and**

   (iii) **Whether they are measured after recognition under the cost model or the revaluation model.**

(d) **The existence and carrying amounts of intangible assets whose title is restricted and the carrying amounts of intangible assets pledged as security for liabilities.**

(e) **The amount of contractual commitments for the acquisition of intangible assets.**

122. When an entity describes the factor(s) that played a significant role in determining that the useful life of an intangible asset is indefinite, the entity considers the list of factors in paragraph 89.

Intangible Assets Measured after Recognition using the Revaluation Model

123. **If intangible assets are accounted for at revalued amounts, an entity shall disclose the following:**

(a) **By class of intangible assets:**

   (i) **The effective date of the revaluation;**

   (ii) **The carrying amount of revalued intangible assets; and**

   (iii) **The carrying amount that would have been recognized had the revalued class of intangible assets been measured after recognition using the cost model in paragraph 73;**

(b) **The amount of the revaluation surplus that relates to intangible assets at the beginning and end of the reporting period, indicating the changes during the reporting period and any restrictions on the distribution of the balance to owners; and**

(c) **The methods and significant assumptions applied in estimating the assets' fair values.**

124. It may be necessary to aggregate the classes of revalued assets into larger classes for disclosure purposes. However, classes are not aggregated if this would result in the combination of a class of intangible assets that includes amounts measured under both the cost and revaluation models.

Research and Development Expenditure

125. **An entity shall disclose the aggregate amount of research and development expenditure recognized as an expense during the period.**

126. Research and development expenditure comprises all expenditure that is directly attributable to research or development activities (see paragraphs 64 and 65 for guidance on the type of expenditure to be included for the purpose of the disclosure requirement in paragraph 125).

Other Information

127. An entity is encouraged, but not required, to disclose the following information:

   (a) A description of any fully amortized intangible asset that is still in use; and

   (b) A brief description of significant intangible assets controlled by the entity but not recognized as assets because they did not meet the recognition criteria in this Standard.

Transition

128. **An entity that has previously recognized intangible assets shall apply this Standard retrospectively in accordance with SLPSAS 3.**

129. **An entity that has not previously recognized intangible assets and uses the accrual basis of accounting shall apply this Standard prospectively. However, retrospective application is permitted.**

130. For intangible items that meet:

   (a) The recognition criteria in this Standard (including reliable measurement of original cost); and

   (b) The criteria in this Standard for revaluation (including existence of an active market);

   an entity may elect to measure an intangible asset on the date of transition, at its fair value and use that fair value as its deemed cost at that date.

131. An entity may elect to use a previous revaluation of an intangible asset at, or before, the date of transition as deemed cost at the date of the revaluation, if the revaluation was, at the date of the revaluation, broadly comparable to:

(a) Fair value; or

(b) Cost or depreciated cost in accordance with SLPSASs, adjusted to reflect, for example, changes in a general or specific price index.

Effective Date

132. **An entity shall apply this Standard for annual financial statements covering periods beginning on or after january 1, 2018. Earlier application is encouraged. If an entity applies this Standard for a period beginning before january 1, 2018, it shall disclose that fact.**

133. When an entity adopts the accrual basis of accounting as defined by SLPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Appendix A

Application Guidance

This Appendix is an integral part of SLPSAS 20.

Website Costs

AG1. An entity may incur internal expenditure on the development and operation of its own website for internal or external access. A website designed for external access may be used for various purposes such as to disseminate information, create awareness of services, request comment on draft legislation, promote and advertise an entity's own services and products, provide electronic services, and sell services and products. A website designed for internal access may be used to store entity policies and details of users of a service, and search relevant information.

AG2. The stages of a website's development can be described as follows:

(a) Planning—includes undertaking feasibility studies, defining objectives and specifications, evaluating alternatives, and selecting preferences;

(b) Application and Infrastructure Development—includes obtaining a domain name, purchasing and developing hardware and operating software, installing developed applications, and stress testing;

(c) Graphical Design Development—includes designing the appearance of web pages; and

(d) Content Development—includes creating, purchasing, preparing, and uploading information, either textual or graphical in nature, on the website before the completion of the website's development. This information may either be stored in separate databases that are integrated into (or accessed from) the website or coded directly into the web pages.

AG3. Once development of a website has been completed, the Operating stage begins. During this stage, an entity maintains and enhances the applications, infrastructure, graphical design, and content of the website.

AG4. When accounting for internal expenditure on the development and operation of an entity's own website for internal or external access, the issues are:

(a) Whether the website is an internally generated intangible asset that is subject to the requirements of this Standard; and

(b) The appropriate accounting treatment of such expenditure.

AG5. This Application Guidance does not apply to expenditure on purchasing, developing, and operating hardware (e.g., web servers, staging servers, production servers, and Internet connections) of a website. Such expenditure is accounted for under SLPSAS 7. Additionally, when an entity incurs expenditure on an Internet service provider hosting the entity's website, the expenditure is recognized as an expense when the services are received.

AG6. SLPSAS 20 does not apply to intangible assets held by an entity for sale in the ordinary course of operations (see SLPSAS 16 and SLPSAS 9) or leases that fall within the scope of SLPSAS 12. Accordingly, this Application Guidance does not apply to expenditure on the development or operation of a website (or website software) for sale to another entity. When a website is leased under an operating lease, the lessor applies this Application Guidance. When a website is leased under a finance lease, the lessee applies this Application Guidance after initial recognition of the leased asset.

AG7. An entity's own website that arises from development and is for internal or external access is an internally generated intangible asset that is subject to the requirements of this Standard.

AG8. A website arising from development is recognized as an intangible asset if, and only if, in addition to complying with the general requirements described in paragraph 28 of this Standard for recognition and initial measurement, an entity can satisfy the requirements in paragraph 55 of this Standard. In particular, an entity may be able to satisfy the requirement to demonstrate how its website will generate probable future economic benefits or service potential in accordance with paragraph 55(d) of this Standard when, for example, the website is capable of generating revenues, including direct revenues from enabling orders to be placed, or providing services using the website, rather than at a physical location using civil servants. An entity is not able to demonstrate how a website developed solely or primarily for promoting and advertising its own services and products will generate probable future economic benefits or service potential, and consequently all expenditure on developing such a website is recognized as an expense when incurred.

AG9. Any internal expenditure on the development and operation of an entity's own website is accounted for in accordance with this Standard. The nature of each activity for which expenditure is incurred (e.g., training employees and maintaining the website) and the website's stage of development or post-development are evaluated to determine the appropriate accounting treatment (additional guidance is provided in the table included at the end of the Illustrative Examples). For example:

(a) The Planning stage is similar in nature to the research phase in paragraphs 52–54 of this Standard. Expenditure incurred in this stage is recognized as an expense when it is incurred;

(b) The Application and Infrastructure Development stage, the Graphical Design stage, and the Content Development stage, to the extent that content is developed for purposes other than to advertise and promote an entity's own services and products, are similar in nature to the development phase in paragraphs 55–62 of this Standard. Expenditure incurred in these stages is included in the cost of a website recognized as an intangible asset in accordance with paragraph AG8 when the expenditure can be directly attributed and is necessary to creating, producing or preparing the website for it to be capable of operating in the manner intended by management. For example, expenditure on purchasing or creating content (other than content that advertises and promotes an entity's own services and products) specifically for a website, or expenditure to enable use of the content (e.g., a fee for acquiring a license to reproduce) on the website, is included in the cost of development when this condition is met. However, in accordance with paragraph 83 of this Standard, expenditure on an intangible item that was initially recognized as an expense in previous financial statements is not recognized as part of the cost of an intangible asset at a later date (e.g., if the costs of a copyright have been fully amortized, and the content is subsequently provided on a website);

(c) Expenditure incurred in the Content Development stage, to the extent that content is developed to advertise and promote an entity's own services and products (e.g., digital photographs of products), is recognized as an expense when incurred in accordance with paragraph 67(c) of this Standard. For example, when accounting for expenditure on professional services for taking digital photographs of an entity's own products and for enhancing their display, expenditure is recognized as an expense as the professional services are received during the process, not when the digital photographs are displayed on the website; and

(d) The Operating stage begins once development of a website is complete. Expenditure incurred in this stage is recognized as an expense when it is incurred unless it meets the recognition criteria in paragraph 28 of this Standard.

AG10. A website that is recognized as an intangible asset under paragraph AG8 of this Application Guidance is measured after initial recognition by applying the requirements of paragraphs 71–86 of this Standard. The best estimate of a website's useful life should be short, as described in paragraph 91.

AG11. The guidance in paragraphs AG1–AG10 does not specifically apply to software development costs. However, an entity may apply the principles in these paragraphs.

Illustrative Examples

These examples accompany, but are not part of, SLPSAS 20.

Recognition and Measurement of an Internally-Generated Intangible Asset

Example Applying Paragraph 63 of this Standard

IE1. An entity developed a new system to schedule court cases more effectively that will result in increased service delivery. During the financial year ending March 31, 20X8, expenditure incurred for the development of the system was Rs.1,000, of which Rs.900 was incurred before March 1, 20X8 and Rs.100 was incurred between March 1, 20X8 and March 31, 20X8. The entity is able to demonstrate that, at March 1, 20X8, the newly developed system met the criteria for recognition as an intangible asset. The recoverable service amount of the system (including future cash outflows to complete the development before it is available for use) is estimated to be Rs.500.

IE2. At the end of the financial year, the developed system is recognized as an intangible asset at a cost of Rs.100 (expenditure incurred since the date when the recognition criteria were met, i.e., March 1, 20X8). The Rs.900 expenditure incurred before March 1, 20X8 is recognized as an expense because the recognition criteria were not met until March 1, 20X8. This expenditure does not form part of the cost of the system recognized in the statement of financial position.

IE3. During the financial year ending March 31, 20X9, expenditure incurred is Rs.2,000. At the end of this financial year, the recoverable service amount of the system (including future cash outflows to complete the system before it is available for use) is estimated to be Rs.1,900.

IE4. As at March 31, 20X9, the cost of the developed system is Rs.2,100 (Rs.100 expenditure recognized at the end of 20X8 plus Rs.2,000 expenditure recognized in the 20X9 financial year). The entity recognizes an impairment loss of Rs.200 to adjust the carrying amount of the developed system before the impairment loss (Rs.2,100) to its recoverable service amount (Rs.1,900). This impairment loss will be reversed in a subsequent period if the requirements for the reversal of an impairment loss are met.

Example Applying Paragraphs 55–65 of this Standard

IE5. An entity is developing a system which produces statistical reports for its internal use and for sale to third-parties. The system is technically feasible, the entity is aware that there is a demand for this type of report and which third-parties are willing to pay for the product and therefore will generate probable future economic benefits. The expenditure attributable to the development of this system can be identified and measured reliably.

Assessing the Useful Lives of Intangible Assets

IE6. The following guidance provides examples on determining the useful life of an intangible asset in accordance with this Standard.

IE7. Each of the following examples describes an acquired intangible asset, the facts and circumstances surrounding the determination of its useful life, and the subsequent accounting based on that determination.

An Acquired Patent with a Finite Useful Life

IE8. Entity A acquires a patent over a formula for a vaccine, from Entity B to secure Entity A's ability to provide free vaccinations to its constituents. The vaccine protected by the patent is expected to be a source of service potential for at least 15 years. Entity A has a commitment from Entity C to purchase that patent in five years for 60 per cent of the fair value of the patent at the date it was acquired, and Entity A intends to sell the patent in five years.

IE9. The patent would be amortized over its five-year useful life to Entity A, with a residual value equal to 60 per cent of the patent's fair value at the date it was acquired. The patent would also be reviewed for impairment.

An Acquired Patent with an Indefinite Useful Life

IE10. Entity A acquires an asset, the patent over a formula for a vaccine, from Entity B to secure Entity A's ability to provide free vaccinations to its constituents. It is expected that the formula will need to be slightly modified every 10 years to maintain its efficacy. There is evidence to support ongoing renewal of the patent. A contract with Entity B stipulates that Entity B will maintain the efficacy of the formula continuously, and evidence supports its ability to do so. The costs to renew the patent and maintain the efficacy of the formula are expected to be insignificant and will be paid to the Entity B when the improvements are made.

IE11. An analysis of product lifecycle studies, and demographic and environmental trends, provides evidence that the patent will provide service potential to Entity A by enabling it to deliver its vaccination program for an indefinite period. Accordingly, the patent would be treated as having an indefinite useful life. Therefore, the patent would not be amortized unless its useful life is determined to be finite. The patent would be tested for impairment.

An Acquired Copyright that has a Remaining Legal Life of 50 Years

IE12. Entity A acquires a copyright from Entity B to enable it to reproduce and sell the copyrighted material on a cost-recovery basis to its constituency. An analysis of the habits of the entity's constituency and other trends provides evidence that the copyrighted material will generate net cash inflows for only 30 more years.

IE13. The copyright would be amortized over its 30-year estimated useful life. The copyright also would be reviewed for impairment.

An Acquired Broadcasting License that Expires in Five Years—Part A

IE14. Entity A acquires a broadcasting license from Entity B. Entity A intends to provide free broadcasting services in the community. The broadcasting license is renewable every 10 years if Entity A provides at least an average level of service to its users of its service and complies with the relevant legislative requirements. The license may be renewed indefinitely at little cost and has been renewed twice before the most recent acquisition. Entity A intends to renew the license indefinitely and evidence supports its ability to do so. Historically, there has been no compelling challenge to the license renewal. The technology used in broadcasting is not expected to be replaced by another technology at any time in the foreseeable future. Therefore, the license is expected to contribute to Entity A's ability to provide free broadcasting services indefinitely.

IE15. Entity B does not recognize its power to grant broadcasting licenses as an intangible asset. The broadcasting license would be treated by Entity A as having an indefinite useful life because it is expected to contribute to the entity's ability to provide free broadcasting services indefinitely. Therefore, the license would not be amortized until its useful life is determined to be finite. The license would be tested for impairment.

An Acquired Broadcasting License that Expires in Five Years—Part B

IE16. The licensing authority subsequently decides that it will no longer renew broadcasting licenses, but rather will auction the licenses. At the time the licensing authority's decision is made, Entity A's broadcasting license has three years until it expires. Entity A expects that the license will continue to provide service potential until the license expires.

IE17. Because the broadcasting license can no longer be renewed, its useful life is no longer indefinite. Thus, the acquired license would be amortized by Entity A over its remaining three-year useful life and immediately tested for impairment.

An Acquired Right to Operate a Public Transit Route Between Two Cities that Expires in Three Years

IE18. Entity A acquires from Entity B a right to operate a public transit route between two cities, which generates revenues. The transit route may be renewed every five years, and Entity A intends to comply with the applicable rules and regulations surrounding renewal. Transit route renewals are routinely granted at a minimal cost and historically have been renewed when the entity that holds the rights to the route has complied with the applicable rules and regulations. Entity A expects to provide transit services on the route indefinitely. An analysis of demand and cash flows supports those assumptions.

IE19. Because the facts and circumstances support the public transit route providing cash flows to Entity A for an indefinite period of time, the intangible asset related to the transit route is treated as having an indefinite useful life. Therefore, the intangible asset would not be amortized until its useful life is determined to be finite. It would be tested for impairment annually and whenever there is an indication that it may be impaired.

An Acquired List of Property Owners

IE20. A local authority (Entity A) acquires a list of property owners from another public sector entity which is responsible for registering property deeds (Entity B). Entity B is at another level of government, and is not part of Entity A's reporting entity. Entity A intends to use the list to generate tax revenues and Entity A expects that it will be able to derive benefit from the information on the acquired list for at least one year, but no more than three years.

IE21. The list of property owners would be amortized over Entity A's best estimate of its useful life, say 18 months. Although Entity B may intend to add property owner names and other information to the list in the future, the expected benefits to Entity A of the acquired list relate only to the property owners on that list at the date Entity A acquired the list. The list of property owners also would be reviewed for impairment by assessing annually and whenever there is any indication that it may be impaired.

Examples Illustrating the Application Guidance

IE22. The purpose of the table is to illustrate examples of expenditure that occur during each of the stages described in paragraphs AG2–AG3 and to illustrate application of paragraphs AG4–AG11 to assist in clarifying their meaning. It is not intended to be a comprehensive checklist of expenditure that might be incurred.

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[2] Although the local authority may intend to add property owners and other information to the database in the future, the expected benefits of the acquired database relate only to the property owners on that database at the date it was acquired. Subsequent additions would be considered to be internally-developed intangible assets, and accounted for in accordance with this Standard.

STAGE/NATURE OF EXPENDITURE	ACCOUNTING TREATMENT
Planning	
• Undertaking feasibility studies; • Defining hardware and software specifications; • Evaluating alternative products and suppliers; and • Selecting preferences.	Recognize as an expense when incurred in accordance with paragraph 52 of this Standard.
Application and Infrastructure Development	
• Purchasing or developing hardware. • Obtaining a domain name; • Developing operating software (e.g., operating system and server software); • Developing code for the application; • Installing developed applications on the web server; and • Stress testing.	Apply the requirements of SLPSAS 7. Recognize as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria in paragraphs 28 and 55 of this Standard.
Graphical Design Development	
• Designing the appearance (e.g., layout and color) of web pages	Recognize as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria in paragraphs 28 and 55 of this Standard.
Content Development	
• Creating, purchasing, preparing (e.g., creating links and identifying tags), and uploading	Recognize as an expense when incurred in accordance with paragraph 67(c) of this Standard to the extent that content

3 All expenditure on developing a website solely or primarily for promoting, advertising, or providing information to the public at large regarding the entity's own products and services is recognized an expense when incurred in accordance with paragraph 66 of this Standard.

4 See footnote 3.

STAGE/NATURE OF EXPENDITURE	ACCOUNTING TREATMENT
information, either textual or graphic in nature, on the website before the completion of the website's development. Examples of content include information about an entity, services, or products, and topics that subscribers access.	is developed to advertise and promote an entity's own services and products (e.g., digital photographs of products). Otherwise, recognize as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria in paragraphs 28 and 55 of this Standard.
Operating	
• Updating graphics and revising content; • Adding new functions, features, and content; • Registering the website with search engines; • Backing up data; • Reviewing security access; and • Analyzing usage of the website	Assess whether it meets the definition of an intangible asset and the recognition criteria set out in paragraph 28 of this Standard, in which case the expenditure is recognized in the carrying amount of the website asset
Other	
• Selling, administrative, and other general overhead expenditure unless it can be directly attributed to preparing the website for use to operate in the manner intended by management; • Clearly identified inefficiencies and initial operating deficits incurred before the website achieves planned performance (e.g., false-start testing); and • Training employees to operate the website.	Recognize as an expense when incurred in accordance with paragraphs 63–69 of this Standard.

[5] See footnote 3

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