Report of the Emerging Economies Group Meeting

December 2017

Emerging Economies Group

The Emerging Economies Group (EEG) was created in 2011 at the direction of the IFRS Foundation Trustees, with the aim of enhancing the participation of emerging economies in the development of IFRS Standards.

This Report of the Emerging Economics Group provides a summary of the 14th EEG meeting held in Sao Paulo, Brazil on 4–6 December 2017, hosted by the Comitê de Pronunciamentos Contábeis of Brazil (CPC).

The EEG meeting was chaired by Amaro Gomes, a member of the International Accounting Standards Board (Board).

Contact

International Accounting Standards Board

30 Cannon Street

London EC4M 6XH

United Kingdom

Tel: +44 (0)20 7246 6410

Fax: +44 (0)20 7246 6411

Website: **www.ifrs.org**

For further information about the Emerging Economies Group click here.

The next Emerging Economies Group meeting will take place on 14–16 May 2018 in Kuala Lumpur, Malaysia.

14th EEG meeting agenda

Agenda topics included:

- Business Combinations Under Common Control (BCUCC)
- Accounting for micro entities
- IAS 12 *Income Taxes*
- Initial measurement of payables when payment is deferred
- IASB Update
- Introduction to IFRS 17 *Insurance Contracts*

The agenda papers for the meeting are available on the IFRS Foundation website: http://www.ifrs.org/groups/emerging-economies-group/#meetings

Opening remarks

Idésio Silva, Chair of the CPC Foundation, gave an address to open the meeting.

Business Combinations Under Common Control

Annamaria Frosi, a member of the IFRS Foundation's staff, provided an update on the work undertaken to date on the BCUCC research project and sought the views of EEG members on: (i) clarifications of the scope of the project; and (ii) methods of accounting for transactions within the scope of the project.

Project update

EEG members discussed the findings of the research and outreach undertaken by the IFRS Foundation's staff on behalf of the Board. The EEG members provided some insights on how BCUCC are accounted for in their respective jurisdictions.

The majority of EEG members said the 'predecessor method' (acquired net assets measured at carrying amount) is used. EEG members further explained that the reasons for application include cost-benefit considerations and the requirements of local legislation.

EEG members also acknowledged diversity in practice as to how the predecessor method itself is applied. In some jurisdictions, comparative information is provided for all combining entities; whereas comparative information is only provided by the 'receiving' entity in other jurisdictions.

EEG members generally agreed that, even if BCUCC are accounted for by applying the predecessor method, fair value information may be relevant for non-controlling shareholders.

None of the EEG members had experience of the 'fresh start' method of accounting (net assets of all combining entities measured at fair value) being applied to account for BCUCC in their jurisdictions.

EEG members also discussed some of the application questions the Board will need to address if the predecessor method is required for some or all transactions within the scope of the BCUCC project. EEG members expressed mixed views on which carrying amounts—those reported by the controlling party or those reported by the transferred party—should be used when applying the predecessor method.

Scope of the project

EEG members welcomed the Board's tentative decision, made at its October 2017 meeting, to include within the scope of the project particular transactions that do not satisfy the description of BCUCC. However, a few members suggested that the Board consider changing the name of the project to better reflect its scope.

EEG members discussed the recommendations on the scope of the BCUCC project, the IFRS Foundation's staff intended to present to the Board in December 2017. Overall, members supported the recommendations.

In response to a question, the IFRS Foundation's staff explained that the Board does not plan to specify which financial statements (consolidated, separate or individual) any accounting requirements developed by the project will apply. However, the Board specified that the BCUCC project will address the accounting from the perspective of the 'receiving' entity.

Methods of accounting

EEG members discussed whether the acquisition method, set out in IFRS 3 *Business Combinations*, or the predecessor method should be used as a starting point to develop accounting requirements for transactions within the scope of the project.

Some EEG members said that in their jurisdictions the predecessor method is considered the appropriate method of accounting for BCUCC; however, they acknowledged that in some circumstances the acquisition method can provide useful information to users of financial statements.

One EEG member argued that BCUCC are different from business combinations not under common control in that the fact that there is no change in ultimate control over the transferred business(es) changes the economics of the transaction. Therefore, in that member's view, the acquisition method is not appropriate for such transactions even if the combining parties are not wholly owned by the controlling party. The method is inappropriate, the member argued, because the predecessor method better reflects the group perspective and that the combining entities are part of the group. The EEG member further noted that fair value information, if needed, could be supplemented into the notes to the financial statements.

Another EEG member observed that fair value measurement is always subject to a certain degree of subjectivity. In that member's view, the reliability of fair value information in a related party transaction can be questionable.

A different EEG member noted that the Board considered the acquisition method to be the appropriate accounting method for all business combinations within the scope of IFRS 3 because that method is consistent with the general accounting model for transactions in which assets are acquired and liabilities are assumed or incurred (paragraph BC24 of IFRS 3). Therefore, in that member's view, the acquisition method should be considered as the conceptual starting point for transactions within the scope of the BCUCC project. That member further noted that IAS 24 *Related Party Disclosures* requires additional disclosures but does not prescribe a different measurement basis for related party transactions.

Some EEG members highlighted that in their jurisdictions entities are required to prepare consolidated financial statements at each level within a group. They suggested that this fact should be considered by the Board in assessing the costs and benefits of different accounting methods.

EEG members further discussed the factors to be considered when selecting an accounting method for different types of transactions within the scope of the project.

Overall, EEG members agreed that the factors identified by the IFRS Foundation's staff should be taken into consideration when developing accounting requirements for transactions within the scope of the project. However, in their view, none of the factors is decisive in determining which method to apply to a particular transaction. Instead, some EEG members suggested that the Board should focus on the information needs of external parties (eg non-controlling interests or prospective shareholders in an initial public offering) affected by the transaction.

Summary

Darrel Scott, a Board member, summarised the discussion:

- the predecessor method can be justified on cost-benefit grounds, especially when no external parties are involved in the transactions;
- the use of the predecessor method can be conceptually justified as it better reflects the group perspective; however
- some EEG members still prefer the acquisition method because this is the method the Board decided to prescribe for business combinations in IFRS 3.

Amaro Gomes encouraged EEG members to undertake their own outreach, both at national and regional level, to contribute to future discussions on BCUCC.

Accounting for micro entities

Severinus Wijaya, on behalf of the Indonesian Financial Accounting Standards Board, presented an overview of the 'Tiers' of Indonesian Financial Reporting. Severinus Wijaya provided an overview of the Standards for entities that are not publicly accountable and which meet the definition and criteria of 'micro', 'small' or 'medium' entities, as defined by Indonesian law.

Severinus Wijaya noted that in setting standards for micro, small and medium entities, it was necessary to balance cost and benefits, the resources available to preparers and the needs of users of the financial statements.

Darrel Scott provided an overview of the Board's approach to micro entities.

The EEG members agreed to continue to discuss the accounting for micro entities at its next meeting with the aim of providing a summary of the key objectives of accounting for micro entities, and the consequential features of an ideal model.

Application topics

IAS 12 *Income Taxes*

Domingo M. Marchese, a member of Federación Argentina de Consejos Profesionales de Ciencias Económicas (FACPCE), presented a paper on the usefulness of IAS 12 *Income Taxes*.

Domingo Marchese addressed the situation in which an entity applies the revaluation model in IAS 16 *Property, Plant and Equipment* to a non-depreciable asset with an indefinitely useful life (eg land in agricultural activity) and a sale is not expected to occur in the foreseeable future.

Domingo Marchese noted that, where a tax authority does not recognise certain revaluations or restatements of assets for tax purposes, significant deductible temporary differences arise. He further noted that, in countries with medium or high inflation, the difference between the tax base and the carrying amount of the non-depreciable asset can be significant.

Domingo Marchese questioned the recognition of a deferred tax liability in these circumstances. He noted that the problem is compounded because IAS 12 does not permit deferred tax liabilities to be discounted.

EEG members discussed the possibility of the Board making a narrow-scope amendment to IAS 12 exempting the recognition of a deferred tax liability in the situation described. EEG members considered that the FACPCE could make a submission to the IFRS Interpretations Committee on this topic.

The EEG members also discussed whether IAS 12 not permitting deferred tax liabilities to be discounted could be addressed in a narrow-scope project. However, EEG members did not consider discounting of deferred tax liabilities could be addressed in a narrow-scope project.

EEG members did not make any recommendation to the Board.

Initial measurement of payable when payment is deferred

Darrel Scott presented a paper on behalf of Financial Reporting Council of South African (FRCSA).

The FRCSA paper noted:

- applying IFRS 9 *Financial Instruments* a financial receivable is measured based on the IFRS 15 *Revenue from Contracts with Customers* transaction price when a payment from a customer is deferred for a reasons other than it being part of a significant financing transaction or when the period between an entity transferring a promised good or service to a customer and when the customer pays for the good or service is less than one year.

The paper contrasted this with:

- the requirement in IFRS 9 that a financial liability is recognised at fair value and the corresponding asset is recognised in accordance with IAS 2 *Inventories*, IAS 16 *Property, Plant and Equipment* or IAS 38 *Intangible Assets* and is not required to be recognised at fair value. (For example, paragraph 32 of IAS 38 states that, if payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent.)

The FRCSA noted that, gross margins can be affected when the asset corresponding to the financial liability is the purchase of goods or services. The FRCSA noted that in environments in which interest rates are high to moderate, not accounting for the time value of money could have a material effect in a period of less than one year. (In South Africa, the current interest rate is 10.5%.)

The FRCSA also expressed concern about the clarity of the wording in IAS 2, IAS 16 or IAS 38, and, in particular, the phrase 'beyond normal credit terms'.

The EEG members agreed with the FRCSA that equivalent accounting is preferable. Before considering whether to submit a request to the IFRS Interpretations Committee, the members agreed to seek the views of other national standard-setters to discover if concerns about the described circumstance are shared widely.

Board Update

Michelle Sansom, an associate director of the IFRS Foundation, presented an overview of the Board's current activities.

IFRS 17 *Insurance Contracts*

Darrel Scott presented an overview of the new Standard on insurance contracts.

Next meeting

The next meeting of the EEG will be held on 14–16 May 2018 in Kuala Lumpur, Malaysia.