

## Report of the Due Process Oversight Committee (DPOC) meeting

10 April 2013

### 1. Update on technical activities

1.1 The DPOC received an update on technical activities. The DPOC noted that it had received several reports that had been submitted to the IASB considering due process steps on a number of projects since the January 2013 meeting.

1.2 The DPOC noted that the IASB had a busy agenda and a busy publication schedule. The DPOC was updated on the progress of the major projects on the IASB's work plan. The Committee focused in particular on the project on **insurance contracts**, where the IASB had agreed to re-expose its proposals, and was aiming to issue an Exposure Draft (ED) in the first half of 2013. The DPOC was presented with a copy of the paper on due process compliance on the project that had been considered by the IASB at its February 2013 meeting. The DPOC was informed of all the due process steps that had been followed on this project and the outreach and fieldwork that had been, and would be, undertaken. The DPOC noted that the IASB was issuing a full ED of the proposed standard on insurance contracts, but was focusing its questions on a number of key areas where changes had been made since the previous exposure document. The IASB confirmed to the DPOC that the effects analysis on the proposals would be included as part of the Basis for Conclusions accompanying the ED. The DPOC affirmed its view that the IASB had complied with all the required due process steps in developing the forthcoming ED.

1.3 The DPOC also reviewed progress on other major projects. The first concerned the project on **financial instruments: impairment**, on which the IASB had issued its ED on expected credit losses in March 2013. As had been reported to the DPOC in January 2013, the approach taken by the IASB differed from that of the US Financial Accounting Standards Board (FASB), which had issued an ED on its own proposals for a current expected credit loss model, in which all lifetime expected credit losses were recognised for all loans from initial recognition. The FASB had extended the comment period on its ED until 31 May 2013, which allowed for some overlap with the IASB's comment period. The two Boards planned to have a joint discussion on the responses to both their proposals, to see if there was common ground to more closely align the approaches and to meet the many calls for the two Boards to develop a converged solution. A question was asked of whether it was true that concerns had been raised as to whether the IASB's proposals were auditable. The IASB was liaising with the accounting firms on the proposals and seeking feedback on this aspect. The DPOC was also informed that this was an important project for both prudential and securities regulators, and that the IASB was engaged in dialogue with them, but that the situation was complicated by the fact that different regulators had different views on the most appropriate approach.

1.4 On **financial instruments: classification and measurement**, the DPOC noted that the comment period on the IASB's ED of limited amendments to IFRS 9 had now closed, with some 90 comment letters having been submitted. The FASB's ED on classification and measurement of financial instruments was still out for comment, but after the closing date the two Boards planned to redeliberate the proposals jointly and to aim to complete the project in 2013. The IASB would keep the DPOC updated on progress and come back to the Committee with a lifecycle review of the

project for its sign-off before completion. On both of these financial instruments' projects, the IASB was trying to conduct outreach targeted on investors and would report the feedback to the DPOC.

1.5 On **leases**, it was noted that the IASB and FASB were looking to re-expose proposals for a common standard in the first half of 2013, with a 120-day comment period. During the comment period, the two Boards planned to conduct additional outreach including with users of financial statements. On **revenue recognition**, which was another joint project with the FASB, the two Boards had completed their redeliberations and were scheduled to issue a final standard in mid-2013. The DPOC noted that the two Boards had come under some pressure to issue on the website a review draft of the proposed final standard, but were not planning to do so, having issued two EDs on the project and undertaken extensive outreach. The two Boards were going through an extended fatal flaw process to ensure that the drafting of the proposed standard was clear and reflected the technical decisions reached.

1.6 The DPOC was also informed of progress being made on other projects that were new to the agenda, in particular the project on the **conceptual framework**, where a Discussion Paper (DP) was targeted for publication in mid-2013. The DPOC noted that the newly-established Accounting Standards Advisory Forum (ASAF) was the IASB's consultative group on this project, and had held its first meeting on 8-9 April 2013. The bulk of that meeting had been devoted to discussing a number of important areas in the project, in particular measurement, financial performance and what should be presented in Other Comprehensive Income (OCI), and the role of uncertainty when considering the definitions of the elements of financial statements. The IASB reported that the ASAF meeting had gone well and that the quality of the debate had been high. The DPOC also considered how feedback from the ASAF would be conveyed to the IASB, noting that (i) the Board member advisors on the conceptual framework project had attended the meeting, (ii) a summary of the ASAF discussions would be prepared and posted on the website, and (iii) a staff paper would be prepared for the IASB. On the scope of the project, it was noted that the IASB did not intend to reopen those parts of the conceptual framework which had been revised in 2010 (relating to the objective of financial reporting and qualitative characteristics of useful information), but that pressure might come to do so.

1.7 The DPOC was also updated on the progress and due progress steps taken on a number of newer projects, in particular those relating to **rate-regulated activities** and the proposed narrow scope amendment to IAS 41 *Agriculture* on **bearer plants**, as well as an overview of **implementation** activities and developments on the **research programme**.

1.8 Finally under this item, the DPOC received an update of the preparation of **education material**. At its January 2013 meeting, the DPOC had considered the review steps put in place to ensure that educational material would not be confused with an IFRS or perceived as being mandatory. The DPOC noted that the review process had worked with regard to the preparation of guidance material to assist those making the judgements necessary to apply the principles in IFRS 11 *Joint Arrangements*. Most reviewers had expressed concerns that a draft of the material would change how IFRS 11 was applied and so the scope and nature of the proposed material was being reconsidered in the light of the comments received.

## **2. Hedge Accounting forthcoming IFRS: due process 'lifecycle' review**

2.1 The DPOC received a report summarising the due process to date on the project, which dated back to 2008 and the development of the DP *Reducing Complexity in Reporting Financial Instruments*, which had included an approach to simplifying hedge accounting. This had been followed by an ED that was published in December 2010. During the comment period of that ED the IASB undertook one of the most extensive outreach programmes it had ever carried out in relation to a project. The DPOC noted that the ED had been well received and that there had been broad support for the overall objective of the proposals seeking to improve the alignment with risk management practices.

2.2 In its deliberations that preceded the ED published in 2010, the IASB decided to deal separately with the issue of macro-hedge accounting (ie accounting for open portfolios of items). It was noted that this decision had received wide support.

2.3 The DPOC noted that the IASB had decided to take an additional non-mandatory due process step by publishing a review draft of the proposed requirements on the IASB's website. This draft had been posted in September 2012 for a period of 90 days both to enable stakeholders to become more familiar with the document prior to its finalisation and as part of a fatal flaw review. As the posting of the draft had not been a formal comment process, this meant that the 40 or so letters that had been received were not posted on the website, but the key issues raised were summarised in a staff paper and considered by the IASB at its January 2013 meeting. The DPOC discussed this issue and was satisfied that the process followed by the IASB had been acceptable, but suggested that the IASB should carefully consider when it was appropriate to use a review draft instead of a re-exposure draft due to the greater transparency resulting from an ED, noting that a review draft had a very limited purpose (as set out in the *Due Process Handbook*).

2.4 It was noted that some stakeholders continued to have concerns with the IASB's technical decisions, in particular its decision not to grandfather all aspects of current practice for accounting for macro hedges until the separate macro hedge accounting project was completed. Some had raised concerns that it would be burdensome for some banks to migrate to IFRS 9 and then potentially migrate to the new macro-hedge accounting model when it was complete. For example, the European Financial Reporting Advisory Group (EFRAG) had submitted a letter expressing such a view. The staff had analysed the position carefully and would be reporting to the IASB at its April 2013 meeting that it considered that the effort of assessing whether 'macro cash flow hedge accounting' practices comply with the new hedge accounting model should not be overly burdensome for those practices that complied with IAS 39. The DPOC considered that all the due process steps had been satisfactorily completed and, subject to the IASB's decision at its April meeting, that the IASB could proceed with the preparation of the Ballot Draft of the new IFRS 9, incorporating the new requirements for hedge accounting.

## **3. Post-Implementation Review of IFRS 8: progress report and review of procedures**

3.1 The DPOC considered the progress made on the post-implementation review (PIR) of IFRS 8 *Operating Segments* and reviewed the procedures followed, given that this was the first PIR to be conducted by the IASB.

3.2 The DPOC reviewed drafts of agenda papers to be presented to the IASB at its April 2013 meeting that covered the following:

- (a) Sources of input to the IFRS 8 PIR, due process and next steps – this paper discussed the three sources of input to the PIR process: public consultation, outreach, and the review of academic literature (the DPOC was also presented with the agenda papers presented to the IASB at its January 2013 meeting that dealt with the review of academic literature on segment reporting). The paper discussed the adequacy of that input and, in particular, the mixed messages received from investors. It included a due process protocol for the PIR of IFRS 8 and set out the next steps in this process;
- (b) Messages received and feedback summary – this paper summarised the key messages received through consultation and the findings from academic research. It included a draft feedback summary, detailing the messages received and the IASB's suggested responses. It also included a brief comparison of the IASB's findings with those of the US Financial Accounting Foundation (FAF) which had recently completed a PIR of the US Standard on operating segments (with which IFRS 8 was converged); and
- (c) Lessons learned about the PIR process – this paper summarised the feedback received on the PIR process itself together with the staff's analysis of how lessons learnt in conducting this PIR might affect the IASB's approach to subsequent PIRs. It also included a brief discussion of the effect that reviewing a converged Standard might have on the PIR process and how the IASB's process compared with that of the FAF.

3.3 The DPOC's discussion focused on a number of key areas. The first concerned **engagement with all types of participants**. Given the particular importance that investors attached to segment reporting, the DPOC noted the efforts undertaken by the IASB to engage with this stakeholder group in conducting the PIR. That said, the DPOC noted that fewer preparers had taken part in the public consultation process of this PIR than would normally be expected to take part in the comment letter processes for EDs published by the IASB. The DPOC discussed the additional outreach that was conducted with preparers, regulators and accounting firms and the need for some of that consultation to be done privately. The DPOC agreed that engagement with all types of participants was an aspect of the PIR process that would need to be tailored to each PIR and that, when each PIR was planned, the population most affected by the application of the Standard should be identified and that a consultation and outreach plan should be prepared to ensure engagement with all types of participants and across all geographical areas.

3.4 In comparing the approaches to PIRs used by the IASB and the FAF, the DPOC noted that value that had been placed by participants in the IFRS 8 PIR to the **transparency of the process**. The DPOC acknowledged that in the outreach conducted some participants wished to remain anonymous in order to express their views and concerns in a candid and confidential manner and that this presented a challenge of how to report the feedback received externally. The DPOC agreed with the IASB that more work needed to be done to consider in a systematic way how the content of feedback received confidentially could be reported publicly and so considered in the formal feedback process without compromising the privacy of the participant. The DPOC noted that the challenge of reporting these confidential discussions was common to most IASB projects. That said, overall the DPOC was content with the very transparent way in which the IFRS 8 PIR had been conducted.

3.5 On the **outcome of the IFRS 8 PIR process**, the DPOC observed that the staff was proposing to the IASB areas that, in its view, warranted further investigation as potential subjects for narrow-focus amendments to IFRS 8 and questioned whether this was too prescriptive and ‘leading the witness’. It was noted that the IASB had the discretion not to accept a staff recommendation and to call for a more fundamental rethink of the Standard if it thought that the evidence provided by the PIR warranted that approach.

3.6 The DPOC also questioned whether the IASB had **sufficient resources** to comply with the requirement to conduct PIRs on the major projects that were currently in the pipeline. It was noted that these PIRs were three or four years in the future and that some of them would be conducted at the same time. If outreach was coordinated across all PIRs in progress, so that each outreach forum gathered information about any Standards that were currently subject to a PIR, it would significantly reduce the burden placed on the IASB and the staff by the evidence-gathering phase of each PIR.

3.7 The DPOC concluded that:

- (a) the IASB had consulted adequately, and engaged with participants in the appropriate forums, in order to provide balanced feedback about the effect of implementing IFRS 8;
- (b) the agenda papers for discussion at the April 2013 meeting of the IASB adequately described the future steps in the PIR process; and
- (c) the agenda papers demonstrated that the IASB had complied with the due process steps required prior to preparing a report on the PIR of IFRS 8.

3.8 In summary, the DPOC’s view was that the process used for the PIR of IFRS 8 had worked well in practice, represented a good start to the PIR process of the IASB, and provided a useful template for future PIRs.

#### **4. Consultative groups: update and DPOC engagement**

4.1 The DPOC received an update on developments related to a number of consultative groups and considered its own engagement with the IFRS Foundation’s Constitutional bodies and consultative groups.

4.2 The DPOC reviewed the proposed composition of a new consultative group that the IASB was setting up on **rate-regulated activities**. A public call for nominations for membership had attracted 39 candidates, of which the IASB was planning to accept 15, together with 3 observers. The DPOC was satisfied that the membership as proposed provided for a satisfactory balance of perspectives, including geographical balance.

4.3 The DPOC noted, and was also content with, a proposed change in membership of the consultative group on **financial instruments**, with one representative from the banking industry of Japan being replaced by another.

4.4 On **engagement**, the DPOC noted that it had a responsibility to monitor the effectiveness of the bodies and consultative groups that supported the IASB. The DPOC discussed, and agreed with, a proposal put forward by the Chairman that a member of the DPOC (or the Director for Trustee Activities on behalf of the DPOC) should observe at least part of a face-to-face meeting of each of the major groups once a year and report back to the Committee to validate the breadth of

attendance and an appreciation of the quality of dialogue. The Chairman noted that he planned to attend the October 2013 meeting of the IFRS Advisory Council and invited DPOC members to submit further attendance suggestions by e-mail.

**5. Update on operations**

The DPOC received a report on the steps that the IFRS Foundation had and was taking to improve the resilience of the technology for recording meetings, following a problem that had arisen during the February meeting of the IASB, which led to a 90-minute education session on the Conceptual Framework not being recorded.

**6. Review of correspondence**

The DPOC noted that no new correspondence cases had been submitted since the January 2013 meeting.

**7. Any other business**

The Chairman of the DPOC requested input and comments from Committee members on the running of DPOC meetings and how they felt due process issues were being handled.