Date

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Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street, 1st floor
GB-LONDON EC4M 6XH

Dear Sir David,

Re: Exposure Draft of Proposed Improvements to IAS

FEE (Fédération des Experts Comptables Européens – European Federation of Accountants) is pleased to submit its comments on the Exposure Draft of Proposed Improvements to International Accounting Standards. FEE as a founding organisation of EFRAG has also contributed to the EFRAG commenting process by submitting our views to EFRAG on their preliminary comments. Where we are in agreement with the EFRAG comments we refer to these comments, where we are in disagreement our own views are put forward. In addition we raise some additional comments.

IAS 1

Question 1: Do you agree with the proposed approach regarding departure from a requirement of an International Financial Reporting Standard or an Interpretation of an International Financial Reporting Standard to achieve a fair presentation (see proposed paragraphs 13-16)?

A majority in FEE supports the IASB decision to retain the "override" provisions but disagrees with the proposal that there should be alternative treatments according to the regulatory framework of the country where the statements are issued. They support in this respect the detailed observations made by EFRAG.

A minority within FEE believes that an override provision may be misused and therefore, instead of an override principle, would prefer additional disclosures to be made where compliance with an IAS is incompatible with presenting a true and fair view.

Question 2: Do you agree with prohibiting the presentation of items of income and expense as 'extraordinary items' in the income statement and the notes (see proposed paragraphs 78 and 79)?

Yes, we support the prohibition of the presentation of items of income and expense as "extraordinary items" in the income statements and in the notes. We support in this respect the detailed observations made by EFRAG.

Question 3: Do you agree that a long-term financial liability due to be settled within twelve months of the balance sheet date should be classified as a current liability, even if an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the financial statements are authorised for issue (see proposed paragraph 60)?

Yes, we agree with the classification of a long-term financial liability due to be settled within 12 months of the balance sheet date. We support in this respect the detailed observations made by EFRAG.

<u>Question 4</u>: Do you agree that:

(a) a long-term financial liability that is payable on demand because the entity breached a condition of its loan agreement should be classified as current at the balance sheet date, even if the lender has agreed after the balance sheet date, and before the financial statements are authorised for issue, not to demand payment as a consequence of the breach (see proposed paragraph 62)?

(b) if a lender was entitled to demand immediate repayment of a loan because the entity breached a condition of its loan agreement, but agreed by the balance sheet date to provide a period of grace within which the entity can rectify the breach and during that time the lender cannot demand immediate repayment, the liability is classified as non-current if it is due for settlement, without that breach of the loan agreement, at least twelve months after the balance sheet date and:

(i) the entity rectifies the breach within the period of grace; or
(ii) when the financial statements are authorised for issue, the period of grace is incomplete and it is probable that the breach will be rectified (see proposed paragraphs 63 and 64)?

Q4(a): Yes, we do agree.
Q4(b)(i): Yes, we agree with non-current classifications if the breach is rectified within the grace period.
Q4(b)(ii): Yes, we agree. We support in this respect the detailed observations made by EFRAG.

<u>Question 5 and Question 6</u>:

Do you agree that an entity should disclose the judgements made by management in applying the accounting policies that have the most significant effect on the amounts of items recognised in the financial statements (see proposed paragraphs 108 and 109)?

Do you agree that an entity should disclose key assumptions about the future, and other sources of measurement uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year (see proposed paragraphs 110-115)?

The disclosures proposed by the IASB are very general in nature, are difficult to be applied in practice and might result in meaningless disclosures. We suggest that the disclosure requirements for judgements and key assumptions should therefore be covered in the relevant standards and be sufficiently specific to avoid boilerplate disclosures. We support in this respect also the observations made by EFRAG.

<u>Other comments</u>

We support the other comments raised by EFRAG in relation to IAS 1. We would like to emphasise that it is disappointing to see the changes made to paragraphs 8 and 9 (which have now become paragraphs 7 and 8) which remove the explicit encouragement previously given to enterprises (now “entities”), to present certain specified information outside the financial statements. We would however not only refer to a management review since the old paragraph 8 also encouraged presentation of:

> “statements such as environmental reports and value added statements, particularly in industries where environmental factors are significant and when employees are considered to be an important user group”.

It seems to be a highly retrograde step, at a time when social and environmental issues are becoming more widely reported, to de-emphasise them in this way. In the case of environmental issues, in particular, the removal of this encouragement appears to be entirely against the spirit of the *European Commission Recommendation of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual report of companies (2001/453/EC)*.

We also strongly support EFRAG comment on the use of the wording "undue cost or effort". We are also of opinion that the previous test of impracticality is more stringent. Guidance on impracticability is needed in order to achieve application consistent throughout the world. Any change would also have to be made in other standards where the "undue cost or effort" is used.

We would like to make the following additional comments.

- IAS 1.22(a): the wording used in the paragraph gives the wrong impression that the review should demonstrate to management whereas it should be management that must be able to demonstrate to other people including the auditor.

- IAS 1.65(o): The use of the words "owners of the parent" is odd and not consistent with the use of the word "capital". We prefer to use the word "shareholders of the parent".

- IAS 1.49: We do not agree with the proposed change. Para. 1.49 stipulates a presentation of assets and liabilities according to the distinction of current and non-current. A presentation of assets and liabilities in order of their liquidity would only be allowed if the liquidity presentation provides more relevant and reliable information. This change would only be reasonable if proof could be given by the Board that the presentation of assets and liabilities according to the distinction of current and non-current leads to a better information of investors. Because both alternatives have advantages and disadvantages, we take the view that both alternatives should be allowed without any restrictions.

IAS 2

Question 1: Do you agree with eliminating the allowed alternative of using the last-in, first-out (LIFO) method for determining the cost of inventories under paragraphs 23 and 24 of IAS 2?

Yes, FEE agrees with the elimination of LIFO.

Question 2: IAS 2 requires reversal of write-downs of inventories when the circumstances that previously caused inventories to be written down below cost no longer exist (paragraph 30). IAS 2 also requires the amount of any reversal of any write-down of inventories to be recognised in profit or loss (paragraph 31).
Do you agree with retaining those requirements?

Yes, FEE agrees with the reversal of write downs of inventories when the circumstances that previously caused inventories to the written down below cost no longer exist. We support in this respect the detailed observations made by EFRAG.

Other comments

We support the other comments raised by EFRAG in relation to IAS 2.

In addition we would like to raise a comment in relation to para 16A. A paragraph similar to 16A should be included for investment properties (see IAS 40.51).

IAS 8

Question 1: Do you agree that the allowed alternative treatment should be eliminated for voluntary changes in accounting policies and corrections of errors, meaning that those changes and corrections should be accounted for retrospectively as if the new accounting policy had always been in use or the error had never occurred (see paragraphs 20, 21, 32 and 33)?

(i) Voluntary changes in accounting policies: FEE agrees with the proposed improvement in relation to voluntary changes in accounting policies and supports the EFRAG answer in this respect.

(ii) Correction of errors: The reference to (the now deleted) para 12 of the Preface seems to imply that in the perspective of the elimination of any reference to materiality when applying IAS, the deletion of the distinction between fundamental errors and other errors appears to make necessary to restate previous information for any errors, however small. The text is now unclear as to what extent materiality can be applied and clarification would be appreciated. Does the IASB intend the treatment to apply for any errors regardless of their size, especially since the IASB itself refers in Q2 to material errors, although paras 32 and 33 of the standard do not and para 35(d) implicitly does? Our view on whether or not the distinction between fundamental errors and other errors can be deleted depends on the resolution of the materiality issue. If materiality is not brought back in the distinction needs to be maintained.

Question 2: Do you agree with eliminating the distinction between fundamental errors and other material errors (see paragraphs 32 and 33)?

See our response to question 1.

Other comments

We support the comments raised by EFRAG in relation to IAS 8.

IAS 10

FEE supports the proposed changes to IAS 10.

IAS 15

FEE supports the withdrawal of IAS 15.

IAS 16

*Question 1: Do you agree that all exchanges of items of **property, plant and equipment** should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably (see paragraphs 21 and 21A)?*

Yes, all exchanges of items of property, plant and equipment should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably. We therefore disagree with the EFRAG response. It is difficult to draw a line between similar and dissimilar items.

An additional issue could be mentioned in this respect. If the acquisition cost is measured at fair value, it is not clear how to account for a difference between the carrying amount and the fair value of the asset given up.

*Question 2: Do you agree that all exchanges of **intangible assets** should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably? (See the amendments in paragraphs 34-34B of IAS 38, Intangible Assets, proposed as a consequence of the proposal described in Question 1.) (Note that the Board has decided not to amend, at this time, the prohibition in IAS 18, Revenue, on recognising revenue from exchanges or swaps of goods or services of a similar nature and value. The Board will review that policy later in the context of a future project on the Recognition of Revenue.)*

Yes, all exchanges of intangible assets should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably. We therefore disagree with the EFRAG response.

Question 3: Do you agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held for disposal (see paragraph 59)?

A majority in FEE does not agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held for disposal. This majority would like to point out the conflict between para 55 and 59 and the definition of depreciation contained in IAS 16.41, which links depreciation to consumption of benefits provided by the asset. If the asset is idle it is not being consumed. However we agree that obsolescence and other aspects of impairment should be taken into account (IAS 16 and IAS 36).

However, some within FEE support the IASB proposals that depreciation should continue and thereby the EFRAG response. The useful lifetime of the asset may need to be adjusted to reflect the reduced deterioration and increased useful life.

Other comments

We support the other comments raised by EFRAG in relation to IAS 16, except for para. 3.

We would like to make the following additional comments:

- Para 21 needs to make clear what is the treatment of the related gains and losses.

- IAS 40 deals with transfers of items to and from investment properties and inventories. It might be useful if IAS 16 dealt with transfers between property, plant and equipment and inventories.

- IAS 16.46 refers to the review of residual value, but it is hidden in the paragraph where as paras 49 and 52 cover separately in black lettered paragraphs review of useful life and review of depreciation method. The review of residual value should also be in a black lettered paragraph (if maintained see our comments above).

- IAS 16.23: we question if the wording in the paragraph is sufficiently clear to avoid misuse. In our view, the standard of performance needs to be assessed compared to the last time it was improved. The proposed wording gives in our view opening to capitalisation of maintenance expenses by referring to assessment "immediately before the expenditure was made".

IAS 17

Question 1: Do you agree that when classifying a lease of land and buildings, the lease should be split into two elements - a lease of land and a lease of buildings? The land element is generally classified as *an operating lease under paragraph 11 of IAS 17, Leases, and the buildings element is classified as an operating or finance lease by applying the conditions in paragraphs 3-10 of IAS 17.*

Yes, FEE agrees with the approach of splitting the lease of a land and a building. It is our experience that there are no practical problems with such a splitting. The value of the building needs anyhow to be determined separately for depreciation purposes. In this respect we support the observations made by EFRAG.

<u>Question 2</u>: Do you agree that when a lessor incurs initial direct costs in negotiating a lease, those costs should be capitalised and allocated over the lease term? Do you agree that only incremental costs that are directly attributable to the lease transaction should be capitalised in this way and that they should include those internal costs that are incremental and directly attributable?

Yes, FEE agrees with the proposal to require capitalisation of lessors' initial direct costs. We support the treatment of initial direct costs in paras 29A, 38 and 44 for respectively finance leases, manufacturer or dealer leases and operating leases. The treatment in relation to finance leases is consistent with the measurement method applied for loans and receivables originated by the enterprise in IAS 39. The treatment in relation to operating leases of recognition as an expense over the lease term is in fact capitalisation of prepaid costs. We can accept this treatment, although it can be questioned if the approach fits with the conceptual Framework.

<u>IAS 21</u>

<u>Question 1</u>: Do you agree with the proposed definition of functional currency as "the currency of the primary economic environment in which the entity operates" and the guidance proposed in paragraphs 7-12 on how to determine what is an entity's functional currency?

Yes, FEE agrees with the proposed definition of functional currency and the guidance provided. We support in this respect the detailed observations made by EFRAG.

<u>Question 2</u>: Do you agree that a reporting entity (whether a group or a stand-alone entity) should be permitted to present its financial statements in any currency (or currencies) that it chooses?

Yes, FEE agrees that a reporting entity should be permitted to present its financial statements in any currency that it chooses. We support in this respect the detailed observations made by EFRAG.

<u>Question 3</u>: Do you agree that all entities should translate their financial statements into the presentation currency (or currencies) using the same method as is required for translating a foreign operation for inclusion in the reporting entity's financial statements (see paragraphs 37 and 40)?

No, we do not agree that the same translation has to be applied to translating the financial statements of a reporting entity from the functional currency to a different presentation currency and to translating a foreign operation for inclusion in the reporting entity's financial statements. In our view, these are different issues that warrant application of different translation methods. The translation of financial statements for the purpose of including the financial statements of a foreign entity in the reporting entity's consolidated financial statements is based upon financial and other economic relationships between the reporting entity and the foreign entity and involves measurement issues as part of the process of drawing up one set of consolidated financial statements. In contrast, economic relationships between the reporting entity and foreign entities are irrelevant when translating the financial statements of the reporting entity from the functional currency (or presentation currency) into one or more different presentation currencies. The latter translations are done on the basis of financial statements already drawn up. We believe that, when translating the financial statements of the reporting entity from the functional currency into a different presentation currency, the closing rate as of the end of the financial year to which the financial statements relate should be used to uniformly translate asset, liability and equity items as well as income and expense recognised in the period.

Accordingly, corresponding figures for prior financial years presented should be translated using the closing rate as of the end of the prior financial year presented in order to maintain, with regard to the translated amounts, consistency between actual prior year figures and those presented as corresponding figures. The closing rates used for translating current year amounts and corresponding figures as well as the fact that the financial statements had originally been drawn up in a different functional currency should be disclosed in the notes (or it might even be discussed whether the heading of the financial statements should clearly indicate the fact the financial statements presented are derived from a translation of financial statements that were drawn up in a different functional currency by multiplying financial statements amounts by a uniform closing rate). These principles would also apply to translation for presentation purposes of the financial statements of a reporting entity that uses the currency of a hyperinflationary economy as its functional currency. Our above approach is based on the view that, irrespective of the number of translations for presentation purposes, one set of financial statements exists that should be clearly identifiable as the 'genuine' financial statements from which all other statements that use a different presentation currency are derived.

In this way, it would not matter whatever presentation currency is chosen since it can easily be recalculated back to the financial statements expressed in the functional currency if the closing rate is used. If the IASB proposed translation is used to arrive at financial statements in presentation currency, restrictions should be introduced to the choice of the presentation currency in that there should be a clear justification for the choice: the presentation currency must be relevant to the operations of the entity or to the majority of its shareholders or to the majority of its creditors. We recognise that there may exist legal requirements to report in a certain presentation currency.

We therefore also disagree with the EFRAG response.

<u>Question 4</u>: Do you agree that the allowed alternative to capitalise certain exchange differences in paragraph 21 of IAS 21 should be removed?

Yes, FEE agrees that the allowed alternative to capitalise certain exchange differences should be removed and supports the EFRAG response in this respect.

<u>Question 5</u>: Do you agree that
(a) goodwill and
(b) fair value adjustments to assets and liabilities
that arise on the acquisition of a foreign operation should be treated as assets and liabilities of the foreign operation and translated at the closing rate (see paragraph 45)?

Yes, FEE agrees with the proposed approach and supports the EFRAG response in this respect.

<u>Other comments</u>

We support the comments raised by EFRAG in relation to IAS 21.

<u>IAS 24</u>

<u>Question 1</u>: Do you agree that the Standard should not require disclosure of management compensation, expense allowances and similar items paid in the ordinary course of an entity's operations (see paragraph 2)?
'Management' and 'compensation' would need to be defined, and measurement requirements for management compensation would need to be developed, if disclosure of these items were to be

required. If commentators disagree with the Board's proposal, the Board would welcome suggestions on how to define 'management' and 'compensation'.

No, FEE does not agree. We strongly support the answer provided by EFRAG. IASB took a retrograde step and provided reasons that are not convincing especially the fact that no definition exists. Management compensations in the current corporate governance are the most frequently occurring related party transactions. In the current financial reporting climate it seems not at all appropriate to delete the existing requirement of disclosure of management compensation.

<u>Question 2</u>: Do you agree that the Standard should not require disclosure of related party transactions and outstanding balances in the separate financial statements of a parent or a wholly-owned subsidiary that are made available or published with consolidated financial statements for the group to which that entity belongs (see paragraph 3)?
(Note that this proposal is the subject of alternative views of Board members, as set out in Appendix B.)

No, FEE does not agree. The Standard should require disclosure of related party transactions and outstanding balances in the separate financial statements of a parent or a wholly owned subsidiary that are made available or published with consolidated financial statements for the group. FEE supports in this respect the detailed observations made by EFRAG.

<u>Other comments</u>

We support the other comments raised by EFRAG in relation to IAS 24.

<u>IAS 27</u>

<u>Question 1</u>: Do you agree that a parent need not prepare consolidated financial statements if all the criteria in paragraph 8 are met?

Yes, we agree that a parent need not to prepare consolidated financial statements if all criteria in para 8 are met. We support in this respect the detailed observations made by EFRAG.

<u>Question 2</u>: Do you agree that minority interests should be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity (see paragraph 26)?

Yes, we agree that minority interests should be presented in the consolidated balance sheet within equity, separately from parent shareholders' equity. We support in this respect the observations made by EFRAG.

<u>Question 3</u>: Do you agree that investments in subsidiaries, jointly controlled entities and associates that are consolidated, proportionately consolidated or accounted for under the equity method in the consolidated financial statements should be either carried at cost or accounted for in accordance with IAS 39, Financial Instruments: Recognition and Measurement, in the investor's separate financial statements (paragraph 29)?
Do you agree that if investments in subsidiaries, jointly controlled entities and associates are accounted for in accordance with IAS 39 in the consolidated financial statements, then such investments should be accounted for in the same way in the investor's separate financial statements (paragraph 30)?

FEE favours retaining all three existing options and supports EFRAG's response in this respect.

Other comments

We support the other comments raised by EFRAG in relation to IAS 27.

In addition, in relation to para 27.32, we note that the original disclosures in (a) of the listing of significant subsidiaries has been deleted without any reasoning being given in the basis for conclusions. This applies also to IAS 28 where the “old” para 27(a) has been deleted. It is not clear to us that IAS 24.12 covers all this information. We therefore advise that para IAS 27.32 and IAS 28.27(a) should be reintroduced since these provided useful information to the users of financial statements.

IAS 28

Question 1: Do you agree that IAS 28 and IAS 31, Financial Reporting of Interests in Joint Ventures, should not apply to investments that otherwise would be associates or joint ventures held by venture capital organisations, mutual funds, unit trusts and similar entities if these investments are measured at fair value in accordance with IAS 39, Financial Instruments: Recognition and Measurement, when such measurement is well-established practice in those industries (see paragraph 1)?

Yes, FEE agrees that for venture capital organisations, mutual funds, unit trusts and similar entities IAS 28 and IAS 31 should not apply to investments that otherwise would be associates or joint ventures if these investments are measured at fair value in accordance with IAS 39. We support in this respect the detailed observations from EFRAG.

Question 2: Do you agree that the amount to be reduced to nil when an associate incurs losses should include not only investments in the equity of the associate but also other interests such as long-term receivables (paragraph 22)?

FEE does not agree with the proposed approach since long-term receivables are covered by the recoverability provisions of IAS 39.

Furthermore we would like to raise the comment that para 8A would have made sense under the old heading “Consolidated Financial Statements” but does not under the new heading “Application of the Equity Method”. Moreover para 24A falls under the heading “Separate Financial Statements”. Clarification is needed.

IAS 33

Question 1: Do you agree that contracts that may be settled either in ordinary shares or in cash, at the issuer’s option, should be included as potential ordinary shares in the calculation of diluted earnings per share based on a rebuttable presumption that the contracts will be settled in shares?

Yes, we agree with the proposed approach and support the EFRAG response in this respect.

Question 2: Do you agree with the following approach to the year-to-date calculation of diluted earnings per share (as illustrated in Appendix B, examples 7 and 12)?

- *The number of potential ordinary shares is a year-to-date weighted average of the number of potential ordinary shares included in each interim diluted earnings per share calculation, rather than a year-to-date weighted average of the number of potential ordinary shares weighted for the period they were outstanding (ie without regard for the diluted earnings per share information reported during the interim periods).*

- *The number of potential ordinary shares is computed using the average market price during the interim periods reported upon, rather than using the average market price during the year-to-date period.*

- *Contingently issuable shares are weighted for the interim periods in which they were included in the computation of diluted earnings per share, rather than being included in the computation of diluted earnings per share (if the conditions are satisfied) from the beginning of the year-to-date reporting period (or from the date of the contingent share agreement, if later).*

No, we support the detailed comments raised by EFRAG which noted considerable flaws in the year-to-date calculation of diluted earnings per share in the examples provided.

Other comments

We support the other comments raised by EFRAG in relation to IAS 33.

IAS 40

Question 1 and Question 2:

Do you agree that the definition of investment property should be changed to permit the inclusion of a property interest held under an operating lease provided that:
(a) the rest of the definition of investment property is met; and
(b) the lessee uses the fair value model set out in IAS 40, paragraphs 27-49?

Do you agree that a lessee that classifies a property interest held under an operating lease as investment property should account for the lease as if it were a finance lease?

No, we do not agree that the definition of investment property should include property interest held under an operating lease. According to IAS 17, only finance leases should be recognised as assets because just a finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset and, hence, leads to economic ownership. It does not seem to be reasonable to make a change in the treatment of operating and financial leases without changing the overall concept of recognising leases. We disagree in this respect with EFRAG.

Question 3: Do you agree that the Board should not eliminate the choice between the cost model and the fair value model in the Improvements project, but should keep the matter under review with a view to reconsidering the option to use the cost model in due course?

Yes, FEE agrees that the option should not be eliminated at this stage and supports the EFRAG response in this respect.

We would be pleased to discuss with you any aspect of this letter you may wish to raise with us.

Yours faithfully,

Göran Tidström
President