CIMA

12 September 2002

International Accounting Standards Board
30 Cannon Street
LONDON
EC4M 6XH

Cc Hans Nailor, Accounting Standards Board

Dear Sirs

IMPROVEMENTS TO INTERNATIONAL ACCOUNTING STANDARDS

Thank you for the opportunity for the Chartered Institute of Management Accountants to comment on the thirteen standards affected by your Improvements project.

The Chartered Institute of Management Accountants (CIMA) is a global professional body specialising in management accounting. CIMA represents over 74,000 students and 57,000 members in 156 countries.

We have reviewed the changes carefully, and would like to express our support for the project and its objectives. Comments on individual standards are given below, both generally and in response to specific questions.

Overall, we feel that the improvements provide a valuable boost to the European convergence project, which will lead to the adoption of International Accounting Standards throughout the EU for listed companies. We look forward to the more difficult issues ahead being handled in the same constructive and sensible way.

This letter has also been sent today in an email, as a Word document.

Yours sincerely

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Proposed Improvements to International Accounting Standard IAS I Presentation Financial Statements

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?*

Yes CIMA agrees with this approach, which essentially introduces a “true and fair” override into international standards for the first time, which CIMA feels is congruous with a principles based-approach. Disclosure of the departure, the rationale, and the financial impact are essential.

2 *Do you agree with prohibiting the presentation of items of income and expense as “extraordinary items” in the income statement and the notes?*

Yes, CIMA agrees with this prohibition.

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?*

Yes, CIMA agrees with this proposal.

4 *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?

(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:

(1) 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?

Yes, CIMA agrees such long-term liabilities should be thus classified.

5 *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?*

CIMA consider that only those judgements that have a significant effect on the financial statements should be disclosed. Additional disclosure, of judgements that do not have a significant effect on the financial statements, would not be useful for users of financial statements adding what might be called information “noise”.

6 *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?*

Yes, CIMA agrees with the disclosure of such key assumptions, for material issues. However, CIMA would want to avoid excessive disclosure, by not referring to risks that apply to all entities; and by allowing cross-referencing to relevant discussion in the Operating and Financial Review, Management Discussion and Analysis or other narrative.

Other general comments:

Clearly a degree of subjectivity is involved in deciding which policies are most significant, and which assumptions are key, but the guidance is clear.

We note that the proposed IAS 1 deletes the former paragraph 6, which states that it is the responsibility of the Board of Directors and/or other governing body, for the preparation and presentation of an entity's financial statements. We think this statement is important, and should be retained in the revised IAS.

Proposed Improvements to International Accounting Standard IAS 2 *Inventories*

I *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?*

We welcome the elimination of the LIFO alternative.

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?

We accept the retention of the requirement to reverse inventory write-downs through the profit and loss account, where appropriate. We would expect circumstances that required such reversals to occur infrequently.

Proposed Improvements to International Accounting Standard IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*

I *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?*

Yes CIMA agrees to the elimination of alternative treatments.

2 *Do you agree with eliminating the distinction between fundamental errors and other material errors?*

Yes CIMA agrees to the removal of the distinction. We would emphasise that correction should be limited to cases of material error only. Small and therefore pointless corrections of accounts will impair both the user's understanding of the accounts and his/her confidence in them.

Proposed Improvement to International Accounting Standard IAS 10 *Events After the Balance Sheet Date*

Although the change, which prohibits the recognition of dividends declared after the balance sheet date, is at variance with current UK practice, it is logical and we support it.

Proposed Improvement to IAS 15 *Information Reflecting the Effects of Changing Prices*

We agree with the withdrawal of this standard. However we would observe that for countries which have significant inflation, but are not hyperinflationary, accounts drawn up under International Accounting Standards can give a distorted picture of the underlying economic situation. The same is true under UK standards and US standards. We have no solution to suggest, but the issue should be kept under review.

IAS 16 PROPERTY, PLANT AND EQUIPMENT

I *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 2 IA of the [draft] FRS on property, plant and equipment)?*

And

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?*

We agree that exchanges of property, plant and equipment, and also of intangible assets should be made at fair value.

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 of the [draft] FRS on property, plant and equipment)?*

Yes. The purpose of depreciation is to take into account the effluxion of time, so it should not cease when an asset is temporarily idle. If an asset is retired, and is not to be used again, it should not be depreciated but held at book value, subject to impairment testing, or written down to estimated disposal value, or reclassified as a current asset depending on the future plans for the asset.

Proposed Improvements to International Accounting Standard IAS 17 *Leases*

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, CIMA agrees the lease should be split thus. Additional explanation may be needed to clarify the accounting treatment of contracts where the UK terminology is confusing. Specifically, property leases in the UK may not be leases in the accounting sense.

2 *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 attributed 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, CIMA agrees these initial costs should be capitalised.

Proposed Improvements to International Accounting Standard IAS 21 *The Effects of Changes in Foreign Exchange Rates*

1 *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?*

CIMA agrees with the definition and the guidance.

2 *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, CIMA agrees that the entity should be permitted to present its financial statements in any currency it chooses. To require otherwise might cause conflict with local Stock Exchange rules.

3 *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)?*

Yes, CIMA agrees that entities should use the same method as they are required to use for translating a foreign operation.

4 *Do you agree that the allowed alternative to capitailse certain exchange differences in paragraph 21 of IAS 21 should be removed?*

CIMA agree to the removal of this alternative.

5 *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, this recommendation ensures such transactions are accounted for in the same currency as the revenue stream, which is logical.

Proposed Improvements to International Accounting Standard IAS 24 *Related Party Disclosures*

We feel this standard should require the disclosure of the controlling party, and the ultimate controlling party. This is information of fundamental importance in understanding the operations of a group.

It is always desirable to keep disclosures as concise as possible, both to minimise costs and more importantly to ensure that key information is not obscured by masses of trivia. The standard should require disclosure of *material* transactions only, and CIMA believe that guidance on what is material in this context is necessary.

I 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)?

We believe management compensation and related items should be excluded from disclosure, as proposed.

2 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)?

Yes, CIMA agree that there should be no requirement to disclose inter-group transactions between or with wholly owned subsidiaries.

CIMA believe that subsidiaries where minority holdings are less than 10% should also be exempted from disclosing inter-group transactions, which it believes will add no value to the accounts. It is clear from the alternative views in the exposure draft that this is a sensitive area. If this is not acceptable to the IASB, then we urge you to seek some lesser exemption, either with a smaller minority ceiling, or limiting the disclosure by type or on the basis of materiality to the individual. The aim should be to avoid trivial disclosures.

Proposed Improvements to International Accounting Standard IAS 27 *Consolidated and Separate Financial Statements*

1 *Do you agree that a parent need not prepare consolidated financial statements if all the criteria in paragraph 8 are met?*

Yes, CIMA agree that a parent need not prepare consolidated financial statements under these conditions.

2 *Do you agree that minority interests should be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity?*

Yes, CIMA agree to minority interests being presented in such a manner.

3 *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?*

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?

Yes, CIMA agree such investments should be accounted for as suggested - at cost or in accordance with IAS39 - in a parent's separate financial statements, and that the treatment adopted in the separate statements and the consolidated accounts should be consistent.

Proposed Improvements to International Accounting Standard IAS 28 *Accounting for Investments in Associates*

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?*

Yes, CIMA agrees that IAS 28 and IAS 31 should not apply to entities in those sectors.

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

Yes, CIMA agree that the parent's share of the accumulated losses of the associate which exceed the investment of the parent in its equity should be set against the other non-current assets of the parent which are liabilities of the associate, until these are also reduced to nil.

Proposed Improvements to International Accounting Standard IAS 33 *Earnings Share*

The requirement in paragraph 65, relegating non-standard earnings per share calculations to the notes to the accounts, and banishing them from the profit and loss account is acceptable. However, we hope that this does not herald a more detailed and restrictive approach to specifying the content of the profit and loss account. CIMA believes entities should have the discretion to add such additional analysis as they, or the users of their accounts, find useful and would be disappointed to see the introduction of further requirements that led to a totally prescribed profit and loss account.

I *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, CIMA agrees to the inclusion of potential share issues arising from transactions which may be settled in shares in the diluted eps calculation.

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 (i.e. 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).*

Yes, CIMA agrees to the technical principles for calculating eps illustrated in the examples.

Proposed Improvements to International Accounting Standard IAS 40 *Investment Property*

1 *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?

CIMA agree that a property interest held under an operating lease may be treated as an investment property under the conditions stated.

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

CIMA agree that a property interest treated as an investment property under those conditions should be accounted for as a finance lease.

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?*

CIMA agree that the choice between the cost model and the fair value model should be kept under review.