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Dear David,

Exposure Draft of Proposed Improvements to IFRSs (Project Cycle 2007-2009)

We appreciate the opportunity to respond to the International Accounting Standards Board's Exposure Draft (ED) 'Improvements to IFRSs' (an ED of proposed amendments to International Financial Reporting Standards) for the second cycle of the Annual Improvements Process (AIP) project. This letter represents the view of the German Accounting Standards Board (GASB).

The GASB supports several changes regarding the process that the IASB decided on in May 2008 after having had its experiences with the first project cycle and the comments received. In particular, we deem it a major improvement that the effective date and the transitional provisions have been provided individually for each amendment in the current ED.

Another decision taken in May 2008 was that the IASB intends to publish post-ballot drafts of each amendment on its website before publishing the ED each year. Publishing post-ballot drafts instead of so-called near final drafts would, from our point of view, enhance the process and reduce the burden for preparers and other parties involved. Unfortunately, the IASB did not publish any draft for its second project cycle on its website before publishing the ED. We expect that the IASB will publish drafts for the third project cycle (2008-2010) on its website during the year as soon as the ballot process has been completed.

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Moreover, we welcome the IASB's intent to structure forthcoming EDs in the same way as the final standard 'Improvements to IFRSs' issued in May 2008 to separate necessary but non-substantive proposals in part II of the document from proposals with higher importance. Unfortunately, the current ED is not structured like this. If this means separation is not necessary because all proposals are of equal importance (i.e. involve accounting changes for presentation, recognition and measurement purposes), we would prefer a corresponding explanatory note in the ED.

Although we support many of the changes made regarding the process and although we see the IASB's efforts to ensure that final 'Improvements to IFRSs' are published at the beginning of April of the particular year following the publication of the ED (to grant at least a nine-month implementation period for the amendments), we deem it still unfortunate that each final version of 'Improvements to IFRSs' is to be published shortly after the annual Bound Volume edition has been issued. This leads to an out-dated version of the printed Bound Volume version only a few weeks after it having been published. Moreover, due to the regular effective date of most of the amendments of the particular 'Improvements to IFRSs' standards at the beginning of the following year, no Bound Volume will ever be up to date at the beginning of any year. We do not favour this outcome and, therefore, suggest reconsidering the timing of future project cycles.

Furthermore, we are not convinced of the IASB's decision also taken in May 2008 that the 'project scope should not be determined by a definition of minor amendments'. We see the difficulties connected with determining an appropriate project scope and the problems with divergent interpretations of 'minor amendments' that caused the aforementioned IASB decision. We furthermore take note of the current amended scope definition: 'non-urgent, but necessary amendments to IFRSs' that is supported by an additional explanation like the following 'to resolve inconsistencies between standards or clarify unclear wording'. To us, this description of the project scope represents a good starting point to understand what the focus of the project is, but this description does not make clear which kind of amendments to IFRSs is permitted to be dealt with through the AIP and which is not. The IASB's announcement that 'the evaluation of whether to publish an amendment as a stand-alone document or with a group of others requires judgement' seems not to be sufficient to us because it remains unclear which criteria the IASB applies in making this evaluation. Even the statement that the IASB 'continues to use a single exposure draft to publish proposed improvements to IFRSs, unless the changes relate to *unusually significant or broad* issues' is too vague to understand how the IASB performs this judgement. Therefore, we think it is important to give a kind of 'limit' in respect of amendments that are permitted to be addressed as part of the AIP project. We are convinced that such 'limit' would considerably enhance the transparency in respect of the AIP project and, therewith, the transparency of the standard-setting process in general. In addition such 'limit' would help to keep and potentially also increase the confidence of all constituents in the IASB's due process.

From our point of view, such 'limit' for amendments to IFRSs that are permitted to be addressed by the AIP project could contain the following factors:

- The amendment is a limited issue (i.e. there are for instance no or no material cross-cutting issues).
- There is no other related project under way at this time or in the near future in which the particular amendment could be addressed.



- The amendment is relevant for constituents, i.e. a necessary amendment from the point of view of the constituents (and not only from the point of view of the IASB).

For comments on the twelve amendments proposed and, in particular, the questions raised in the ED, we refer to the appendix to this cover letter. In summary, we basically agree with most of the proposals contained in the ED. In some cases, though we agree in principle, we have provided additional comments that could, from our point of view, further improve the amendments.

However, in one case we disagree with the proposed amendment to the standard for reasons also set out in detail in the appendix to this letter. This issue concerns the proposal to amend IAS 7 in respect of the classification of expenditure on unrecognised assets. One reason for our rejection of the proposed amendment is that we think the issue is not sufficiently limited for being addressed within the AIP project. This is because there is an active project under way – the Financial Statement Presentation project where recently a Discussion Paper was submitted – which will affect the issue that the IASB currently proposes to amend by the AIP project. Therefore, we would prefer this issue to be addressed in connection with the Financial Statement Presentation project rather than the AIP project.

If you would like to discuss any aspects of this comment letter in more detail, please do not hesitate to contact me.

Yours sincerely,

Liesel Knorr

President



Appendix

General questions (applicable to all proposed amendments)

Question 1 – Do you agree with the Board's proposal to amend the IFRS as described in the exposure draft? If not, why and what alternative do you propose?

Question 2 – Do you agree with the proposed transition provisions and effective date for the issue described in the exposure draft? If not, why and what alternative do you propose?

Proposed amendment to International Financial Reporting Standard 2 *Share-based Payment*

Scope of IFRS 2 and revised IFRS 3

We agree with the proposed amendment regarding IFRS 2.5 in order to confirm that the contribution of a business on formation of a joint venture and common control transactions are not within the scope of IFRS 2.

We also agree with the proposed effective date of 1 July 2009 as the amendment results from the revising of IFRS 3 and, thereby, represents a kind of consequential amendment. That it has the same effective date as IFRS 3 (revised 2008) seems, therefore, to be reasonable. The short implementation period is acceptable because the amendment merely confirms current accounting practice rather than changing it. Based on this premise, we furthermore consider a retrospective application appropriate.

Proposed amendment to International Financial Reporting Standard 5 *Non-current Assets Held for Sale and Discontinued Operations*

Disclosures of non-current assets (or disposal groups) classified as held for sale or discontinued operations

In principle, we agree with the proposal to amend IFRS 5 in order to clarify that IFRS 5 specifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations, which means that disclosures in other IFRSs do not apply to such assets (or disposal groups) unless those IFRSs specifically require disclosures in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations.

However, we think that the explanation given in the Basis for Conclusions to the proposed amendment, in particular in BC4, might lead to confusion in respect of the meaning of the amendment. Some might, furthermore, take the view that the statement in BC4 contradicts what IFRS 5.5A is supposed to say. In our view it is at least not completely clear what is exactly meant by the statement in BC4 that 'disclosures about measurement of those assets and liabilities [i.e. assets and liabilities included in a disposal group but not within the scope of the measurement requirements of IFRS 5] are normally provided in the other notes to the financial statements'. In particular, it remains unclear which disclosures are required to be provided in other notes and what



‘normally’ does mean in this context. We therefore would appreciate a respective clarification.

Apart from that, we agree with the proposed effective date of 1 January 2010 and with a prospective application of the amendment. Furthermore, we particularly appreciate the amendment being early applicable as this will be of benefit for those entities that until now interpreted IFRS 5 in a different way and therefore provided more disclosures than necessary.

Proposed amendment to the Basis for Conclusions on International Financial Reporting Standard 8 *Operating Segments*

Disclosure of information about segment assets

We fully support the proposed amendment to the Basis for Conclusions accompanying IFRS 8 that clarifies that making no disclosure of segment assets would be in accordance with IFRS 8. We agree that this view complies with long-standing interpretations issued in the US for the application of SFAS 131 and, moreover, with the management approach underlying IFRS 8. However, we think that BC35 sentence 4 would be more precise if it stated: ‘Therefore, making no disclosure of segment assets would be in accordance with the IFRS in all cases information on segment assets is not provided to the chief operating decision maker.’

Furthermore we take the view that amending the standard itself in addition to the Basis for Conclusions would further enhance the clarity of this aspect. On the one hand we understand that the IASB intended not to diverge in IFRS 8.23 sentence 1 from the wording in the corresponding SFAS 131.27 sentence 1. On the other hand, there are already differences between SFAS 131 and IFRS 8. One of these differences concerns the requirement in IFRS 8.23 sentence 2 to disclose the measure of liabilities for each reportable segment. However, this requirement is explicitly limited in IFRS 8.23 sentence 2 to the situation that the measure of liabilities is reported to the chief operating decision maker. Because this requirement furthermore follows directly the disclosure requirement regarding segment assets, the difference between sentence 1 and 2 in IFRS 8.23 could imply an intended difference in respect of being a minimum disclosure in a segment report. We would, therefore, prefer removing this potential for misinterpretation by amending sentence 1 accordingly or by connecting sentences 1 and 2 in a meaningful manner.

Proposed amendment to International Accounting Standard 7 *Statement of Cash Flows*

Classification of expenditures on unrecognised assets

We do not agree with the proposed amendment regarding IAS 7 in order to state explicitly that only expenditure that results in a recognised asset can be classified as a cash flow from investing activities for the following reasons:

Firstly, we think that classification in the statement of cash flows should not be driven by the accounting but rather by the business of the particular entity. In our view, this better meets the objective of the statement of cash flows to provide users of financial statements information that enables them to evaluate the entity’s ability to generate cash and cash equivalents and the timing and certainty of their generation.



Furthermore, we note that the proposed amendment does not only affect exploration and evaluation expenditures which triggered the proposed amendment. For example, initial expenditures for development activities that do not meet the recognition criteria according to IAS 38 would be allocated to 'operating activities' under the proposed amendment. However, we think that these expenditures could also have been made as part of an entity's investing activities. Therefore, requiring to classify such expenditures in all cases as cash flows from operating activities does not seem to be appropriate.

Lastly, the GASB takes the view that the amendment should not be made without considering conceptual aspects. To us the IASB's convergence argument for the proposed amendment is not sufficient to justify this change. In summary, we therefore think that this amendment should not be addressed as a part of the AIP project but rather in connection with the Financial Statement Presentation project.

Proposed amendment to Appendix of International Accounting Standard 18 Revenue

Determining whether an entity is acting as a principal or as an agent

Specific question

Question 3 – The board proposes to include in the Appendix of IAS 18 *Revenue* guidance on determining whether an entity is acting as a principal or as an agent. What indicators, if any, other than those considered by the Board should be included in the guidance proposed?

We basically support the proposed amendment to the guidance accompanying IAS 18 that addresses the issue of determining whether an entity is acting as a principal or as an agent because the current IAS 18 and accompanying guidance do not contain sufficient material for preparers to make this decision. We also agree with the approach to base this determination on risks and rewards. To additionally provide several criteria that alone or in combination indicate that an entity has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services is helpful in determining whether the entity is acting as a principal or as an agent.

However, the indicators given in the proposed guidance seem to focus on certain kinds of transactions, in particular on the sale of physical goods where payment is to be made after delivery. We take this view because there is, for example, no inventory risk in connection with a service contract or no credit risk when payment has been made in advance. Although we see that the criteria mentioned may indicate, individually or in combination, that an entity is acting as a principal, we would prefer a more general wording in a manner that makes clear: if there is/are 'whatever' risk(s) associated with the respective contractual arrangement, then the entity that has an exposure to the majority of that/those risk(s) is acting as a principal. In our view, this type of wording would better correspond with various kinds of real-life transactions.

In addition, we think that 'changing/bundling the goods or services before reselling' is an important feature that may indicate that the entity is acting as a principal and should, therefore, be explicitly stated in the list of indicators in the Appendix to IAS 18.



Finally, we would like to point out that we would prefer this guidance being placed in the standard instead of the non-authoritative appendix.

Proposed amendment to International Accounting Standard 36 *Impairment of Assets*

Unit of accounting for goodwill impairment

We agree with the proposal to amend IAS 36 in order to clarify that the largest unit for goodwill allocation permitted by IAS 36 is the operating segment level as defined in paragraph 5 of IFRS 8 *Operating Segments* before the aggregation permitted by paragraph 12 of IFRS 8.

We also agree with the proposed effective date of 1 January 2010 and basically with a prospective application of the amendment. However, we would appreciate if the IASB provides the option to retrospectively apply the amendment. In our view retrospective application could be relevant for entities that have to recognise an additional impairment loss due to the amendment because it requires them to test for impairment at a lower level than before. We think that presenting such impairment loss in the prior period(s), i.e. the period(s) in which the impairment happened, would be the more appropriate accounting in respect of the true and fair view principle rather than fully presenting it in the period when the amendment becomes effective.

Proposed amendments to International Accounting Standard 38 *Intangible Assets*

Additional consequential amendments arising from revised IFRS 3

We agree with the proposed amendments to IAS 38.36 and .37 that clarify the effects of decisions made in the Business Combinations project on the accounting for intangible assets acquired in a business combination.

We also agree with the proposed effective date of 1 July 2009 as the amendment is a consequential amendment triggered by IFRS 3 (as revised in 2008). To establish the same effective date as IFRS 3 (revised 2008), therefore, seems to be reasonable. The short implementation period is acceptable because the amendment represents merely a clarification of decisions formerly made in the Business Combinations project. Furthermore, we agree with the proposal regarding a prospective application.

Measuring the fair value of an intangible asset acquired in a business combination

We basically agree with the proposed amendment that clarifies the description of valuation techniques commonly used by entities when measuring the fair value of intangible assets acquired in a business combination that are not traded in active markets. If an IFRS contains the description of valuation techniques it is important that this description is accurate in order to avoid misinterpretation.

However, we do think that it is not necessary to describe valuation techniques in detail in an IFRS. We believe it would be sufficient to provide general requirements that such valuation techniques have to meet in order to comply with IFRSs. If this view is followed IAS 38.41 could be removed from IAS 38 and accordingly the proposed amendment would not be necessary.



Irrespective of this position, we agree with the proposed effective date of 1 January 2010 and a prospective application of the amendment.

Proposed amendments to International Accounting Standard 39 *Financial Instruments: Recognition and Measurement*

Scope exemption of business combination contracts

We are basically in agreement with the proposed amendment to IAS 39.2(g) that clarifies that the scope exemption in the aforementioned paragraph applies only to binding (forward) contracts between an acquirer and a vendor in a business combination to buy an acquiree at a future date. We furthermore agree with the proposed effective date of 1 January 2010 and with a prospective application of the amendment.

However, there are contractual agreements that are substantially identical with forward contracts, i.e. the economic results are the same as with 'real' forward contracts. An example for such contractual agreement is the combination of a put and a call option contract with both having the same strike. We think that all contractual agreements that are substantially identical with 'real' forward contracts should be covered by the scope exemption in IAS 39.2(g). Therefore, we would appreciate a respective modification of the proposed amendment to IAS 39.2(g).

Irrespective of this position, we would appreciate a requirement to disclose such agreements on future business combinations that are encompassed by the scope exemption and therefore excluded from accounting as we see that neither IFRS 3.59 (revised 2008) nor IAS 10.22 will require such disclosure if the acquisition date is after the financial statements have been authorised for issue (and not only after the end of the reporting period).

Application of the fair value option

We fully agree with the proposal that clarifies that the fair value option as stated in IAS 39.11A applies only to financial instruments within the scope of IAS 39 that contain embedded derivatives. We also agree with the proposed effective date of 1 January 2010 and a prospective application of the amendment.

In addition, we would suggest replacing the term 'contract' in IAS 39.11A(a) by 'financial instrument' and specifying the term 'hybrid (combined) instrument' in IAS 39.11A(b) by 'hybrid (combined) *financial* instrument' to make the paragraph fully clear and consistent.

Cash flow hedge accounting

We agree with the proposed clarification that the gains and losses on hedging instruments should be reclassified from equity to profit or loss as a reclassification adjustment in the period or periods that the hedged forecast cash flows affect profit or loss. In addition, we agree with the proposed effective date of 1 January 2010 and a prospective application of the amendment.

As IAS 39.97 and .100 after having been amended require the same accounting for gain and losses that had been recognised in other comprehensive income, we think two



separate paragraphs are no longer necessary and IAS 39.97 and .100 could therefore be combined into one paragraph.

Bifurcation of an embedded foreign currency derivative

We support the purpose of the proposed amendment that is to clarify what the 'economic environment' is in determining whether a currency is commonly used in contracts to buy or sell non-financial items and therefore whether it is closely related to the host contract.

However, we think that the proposal does not achieve the intended clarification. In particular, we wonder how IAS 39.AG33(d)(i) and IAS 39.AG33(d)(iii) relate to each other under the proposed amendment. IAS 39.AG33(d)(i) specifies that 'the *functional currency* of any substantial party to that contract' is a currency which effects that an embedded foreign currency derivative meets the condition of being closely related if payments required by this derivative are denominated in such currency. To us this requirement seems to be already encompassed by the amended (new) requirement in IAS 39.AG33(d)(iii) that states that 'a currency that has one or more of the characteristics of a *functional currency*, as set out in paragraph 9 of IAS 21, of a substantial party to the contract' is a currency with the aforementioned effect. Under the proposed amendment, IAS 39.AG33(d)(i), therefore, seems to be redundant.

A similar issue arises with regard to IAS 39.AG33(d)(ii) which specifies that in cases where an embedded foreign currency derivative requires payments denominated in a 'currency in which the price of the related good or service that is acquired or delivered is routinely denominated in commercial transactions around the world (such as the US dollar for crude oil transactions)', that embedded foreign currency derivative meets the condition of being closely related to the host contract. However, the currency described in IAS 39.AG33(d)(ii) seems already to be covered by the amended (new) IAS 39.AG33(d)(iii) because the Basis for Conclusions for the proposed amendment explicitly provides the description mentioned above as an example for foreign currencies that have one or more of the characteristics of a functional currency as set out in IAS 21.9. Thus, IAS 39.AG33(d)(ii) would also be redundant.

We would like to stress again that we fully support the objective of the proposed amendment. But in the light of the observations explained above, we would suggest redrafting the proposed amendment to fully achieve the necessary clarification.

Irrespective of this issue, we see room for improvement regarding the effective date of the proposed amendment and the transitional provisions. It remains unclear to us what the requirement 'to apply [.. the] amendment[..] prospectively for annual periods beginning on or after 1 January 2010' means for existing contracts with embedded derivatives that have been bifurcated before and, due to the amendment, must not be separated in the future. In this case 'prospective application' could be interpreted as if requiring to stop to account for existing contracts with embedded derivatives separately that have hitherto been accounted for separately (view 1). It could also be interpreted as a requirement that only contracts entered into on or after the amendment's date of first-time application are affected by the amendment, while the accounting for all existing contracts is retained, i.e. those derivatives will continue to be accounted for separately until they are due (view 2). The latter view could be better reflected by a requirement that the amendment regarding IAS 39.AG33(d)(iii) applies to '*contracts entered into in*



annual periods beginning on or after 1 Januar 2010'. We would prefer this alternative and therefore suggest changing IAS 39.103H in a corresponding manner.

We prefer this view 2, as view 1 gives rise to the question of how the change from a previously bifurcated derivative to non-bifurcation should be accounted for: Suppose an embedded derivative that has previously been accounted for separately at fair value with changes recognised in profit or loss is now (prospectively) not required to be bifurcated any longer. The question that follows is: How is the fair value of the derivative as of the date of adoption of the amendment (i.e. non-bifurcation) to be accounted for? Absent explicit requirements on this issue we would think that, as the changes in fair value of the derivative have been recognised in profit or loss, the current carrying amount as of the date of the adoption must be closed out against profit or loss as well. We have strong concerns that this accounting treatment is appropriate and provides decision-useful information.