Organisation internationale des commissions de valeurs
International Organization of Securities Commissions
Organización internacional de comisiones de valores
Organização internacional das comissões de valores

OICV / IOSCO

June 17, 1994.

Mr. Eiichi Shiratori, Chairman
International Accounting Standards Committee
167 Fleet Street
London EC4A 2ES
England

Dear Mr. Shiratori:

The International Organization of Securities Commissions (IOSCO) Working Party No. 1 on Multinational Disclosures and Accounting and its Accounting and Auditing Subcommittee ("Working Party") have reviewed the standards recently revised in the E32 Comparability/Improvements Project of the International Accounting Standards Committee (IASC). This review has been undertaken in the context of the Working Party's assessment of the IASC standards as one alternative to the use of a regulator's domestic standards that the regulator could accept for foreign enterprises entering the regulator's domestic securities market. As discussed in our letter to you of August 16, 1993, the goal of IOSCO is the development of a comprehensive body of international accounting standards that could be used by companies seeking to raise capital or list in the global capital markets. The recently amended E32 standards are part of the core standards identified in our August 16 letter as necessary components of such a comprehensive body of international standards.

The Working Party is pleased to advise you that in its review of the core standards, it would view the following E32 standards, subject to the suspense issues noted, as acceptable.

1. IAS 2, Inventories.
2. IAS 8, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies.
3. IAS 11, Construction Contracts.
4. IAS 16, Property, Plant and Equipment.
5. IAS 18, Revenue.

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6. IAS 21, The Effects of Changes in Foreign Exchange Rates.

7. IAS 22, Business Combinations.

8. IAS 23, Borrowing Costs.

The specific analysis and suspense issues are set forth in Appendix I. Final endorsement of the above standards for use in cross-border listings and offerings is dependent on IOSCO's assessment of the total package of core standards. By separate letter accompanying this letter, the Working Party has set out its views with respect to the IASC standards that were not revised as part of the E32 project.

With respect to the two remaining E32 standards, the Working Party has been unable to reach a consensus on the acceptability of IAS 9, Research and Development Costs, particularly regarding the required capitalization of development costs when specified criteria are met. In addition, the IASC has acknowledged, and the Working Party concurs, that further improvements to IAS 19, Retirement Benefit Costs, are necessary.

With respect to each standard, suspense issues have been identified by the Working Party. Suspense issues include items that generally are encountered infrequently, often are complex, and would not need to be addressed before IOSCO would consider recommending acceptance of IASC standards. In such cases, IOSCO members may accept compliance with the international accounting standard, accept home country treatment, or require specific host country treatment or equivalent disclosure. In addition, there are some suspense issues that represent reservations of certain member countries on the necessity of full application of international standards. The IOSCO Working Party will review these suspense issues to consider whether it can recommend an interim method of dealing with the issues.

The Working Party believes it now is current with respect to consideration of completed IASC standards and will continue following ongoing IASC projects and plans closely. We would be pleased to meet with you and other IASC representatives, if you wish, to discuss further any Working Party determinations and recommendations to date.

Sincerely,

Linda C. Quinn
Chairman, Working Party No. 1
IOSCO

Michael Meagher
Chairman, Accounting and Auditing Subcommittee
IOSCO

Enclosures

cc: David Cairns, Secretary General
International Accounting Standards Committee

June 17, 1994
APPENDIX I

EVALUATION OF E32 STANDARDS
IOSCO WORKING PARTY NO. 1 AND ACCOUNTING SUBCOMMITTEE

A. IAS 2 (Revised 1993) Inventories

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

a. The benchmark treatment of FIFO or weighted average cost is acceptable, subject to suspense issues.

b. The allowed alternative treatment of LIFO is acceptable, subject to suspense issues.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues [1]/

a. None.

3. Suspense Issues [2]/

a. Some IOSCO member countries may accept the inventory method described in Article 38 of the EC 4th Directive.

b. One member country believes that measurement at the lower of cost and net realizable value should not be enforced and measurement at the historical cost should be allowed.

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[1]/ Essential issues are matters that certain IOSCO members believe need to be dealt with by the IASC to obtain a reasonably comprehensive set of international accounting standards.

[2]/ Suspense issues include items that generally are encountered infrequently, often are complex, and would not need to be addressed before IOSCO would consider recommending acceptance of IASC standards. In such cases, IOSCO members may accept compliance with the international accounting standard, accept home country treatment, or require specific host country treatment or equivalent disclosure. In addition, there are some suspense issues that represent reservations of certain member countries on the necessity of full application of international standards.

c. One member country believes that measurement at replacement cost should be allowed.

d. One member country believes that the last purchase price method should be allowed for the sake of convenience in cases where it approximates historical cost on a consistent basis.

e. Some member countries believe that the reconciliation between the benchmark treatment and the allowed alternative treatment should not be required when applying LIFO.

4. Potential Long-Term Projects [3]

a. Consider developing guidance on the application of the LIFO method.

B. IAS 8 (Revised 1993) Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

a. The benchmark treatment of retroactive restatement for fundamental errors and changes in accounting policies is acceptable, subject to suspense issues.

b. The allowed alternative treatment for fundamental errors and changes in accounting policies of inclusion in profit or loss for the current period and presentation of pro forma information for current and prior periods as if retroactively restated is acceptable, subject to suspense issues.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

a. None

3. Suspense Issues

a. Consider recognition and measurement issues and reconsider disclosure and presentation issues for discontinued operations and other restructurings. Discontinued operations is one of the IOSCO core standards that should be considered.

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[3] Potential long-term projects are other matters that eventually should be considered by the IASC to enhance overall comparability and transparency of financial statements.

b. The requirement in paragraph 46 to follow transition and effective date requirements in IASC standards resulting in a change in accounting policies (or even just new disclosures) would be considered on a case by case basis. Because many international standards are being revised in a relatively short period of time, certain members of IOSCO are concerned about the comparability of financial statements with prior periods if the required impacts of the changes were not disclosed for all periods.

c. Some IOSCO member countries may not require the pro forma information required by the allowed alternative treatment with respect to changes in accounting policies and fundamental errors.

4. Potential Long-Term Projects

a. Consider the accounting treatment for changes in accounting estimates, e.g., retrospective versus prospective treatment.

C. IAS 9 (Revised 1993) Research and Development Costs

1. Evaluation of Required Treatments

a. IOSCO Working Party No. 1 has been unable to conclude on the acceptability of the required treatment of capitalization of development costs as an asset, when specified criteria are met. Some IOSCO member countries may require disclosures providing information equivalent to a treatment of expense of all development costs, whereas other IOSCO member countries may require or allow development costs to be expensed without reconciliation. One member country believes that research cost and development cost should not be accounted for separately and it should be acceptable to recognize such costs as either assets or expenses.

b. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to the suspense issue.

2. Essential Issues

a. See item C.1.a. above.

3. Suspense Issue

   a. Some IOSCO member countries may allow amortization of capitalized development costs to commence in the year following capitalization.

4. Potential Long-Term Projects

   a. Reconsider the required treatment of capitalization of development costs as an asset when specified criteria are met or consider providing more objective criteria for required capitalization.

D. IAS 11 (Revised 1993) Construction Contracts

1. Evaluation of Required Treatments

   a. The required treatment of the percentage of completion method for construction contracts is acceptable, subject to suspense issues.

   b. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

   a. None.

3. Suspense Issues

   a. Some IOSCO member countries may condition acceptance by specifying a treatment for the determination of the expected loss that would require a consistent treatment for indirect costs. Paragraph 36 of IAS 11 (revised) does not specify how the "expected loss" is to be determined and could be interpreted to exclude indirect costs despite guidance in paragraphs 26 and 33 that would appear to require that indirect costs be included.

   b. Some IOSCO member countries may not require a reconciliation between the completed contract and percentage of completion method when the completed contract method is used.

4. Potential Long-Term Projects

   a. None.

E. IAS 16 (Revised 1993) Property, Plant and Equipment

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

a. The benchmark treatment of cost less accumulated depreciation is acceptable, subject to suspense issues.

b. Allowed alternative treatment - see suspense issue E.3.a. following.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

a. None.

3. Suspense Issues

a. Some IOSCO member countries may condition acceptance of the allowed alternative treatment of revalued amounts (fair value) less subsequent accumulated depreciation on the disclosure of information providing significant balance sheet and income statement effects of revaluation (instead of just the balance sheet as required by the standard).

b. Consider eliminating alternatives for identifying and measuring impairment of the cost or carrying amount of long-lived assets in a project that also would consider identifiable intangibles and goodwill. Paragraphs 56 to 58 of the standard do not provide sufficient guidance to achieve reasonably comparable results in identifying impairment or for measuring the recoverable amount, e.g., should discounting or fair values be considered.

c. In reference to paragraph 62, consider a more complete discussion of the surrounding circumstances which indicate there has been a disposal of assets. The sale treatment and corresponding potential gain recognition on disposal of operating assets, businesses, or non-performing assets is dependent upon evaluation of factors involved in a particular transaction. These factors may include continuing involvement, dependence upon future successful operations of the acquiror for realization, and guarantees, recourse obligations, and participation in the rewards of ownership.

d. In the past certain revaluations were required by law due to severe inflation in the countries concerned. The Working Party may determine that such revaluations would not necessitate the disclosure of significant balance sheet and income statement effects provided that the years and amounts of the revaluations were disclosed.

e. One member country believes that in the recognition of property, plant, and equipment, the receipt of funds furnished by customers for acquisition of equipment, as an indemnity for expropriation of assets, insurance money, and an item of property, plant and equipment acquired as a result of involuntary conversion (for example, pursuant to government and public campaign to dislocate a plant or office from a designated urban area to a non-urban area for such reason as urban development), as well as for the acquisition of assets by government grant, should be allowed to be accounted for as deductions in arriving at the carrying amount of the assets, or to be recognized fully in the income statement at the time when received.

4. Potential Long-Term Projects

a. Environmental accounting issues.

F. IAS 18 (Revised 1993) Revenue

1. Evaluation of Required Treatments

a. The required treatment of the percentage of completion method for transactions involving the rendering of services is acceptable, subject to suspense issues.

b. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

a. None.

3. Suspense Issues

a. Consider revenue recognition issues involved with various transportation industries.

b. Consider whether the guidance for real estate sales in item 9 of the Appendix is sufficient for enterprises in the real estate industry, as opposed to occasional sales of real estate.

c. Consider revenue recognition and other specialized industry accounting and disclosure issues that may apply to the aforementioned transportation and real estate industries and various other specialized industries such as financial institutions, insurance, oil and gas, mining, agriculture, forestry, rate-regulated utilities, commodities dealers, computer software, investment companies, broker-dealers, venture capitalists, motion picture production, broadcasting, cable television, records and music, health care providers, casinos, and insurance brokers. The IOSCO Accounting Subcommittee and IOSCO Working Party No. 1 as yet have not considered the adequacy of the core standards with respect to the above industries.

d. Some IOSCO member countries may not require a reconciliation between the completed contract and percentage of completion methods when the completed contract method is used.

4. Potential Long-Term Projects

a. None.

G. IAS 19 (Revised 1993) Retirement Benefit Costs

1. Evaluation of Required, Benchmark and Allowed Alternative Treatments

a. The benchmark treatment of an accrued benefit valuation method is acceptable, subject to the essential and suspense issues.

b. Allowed alternative treatment - see suspense issue G.3.a. following.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to the essential and suspense issues.

2. Essential Issues

a. The IASC has acknowledged and IOSCO Working Party No. 1 concurs that further improvements to IAS 19 are necessary. The most significant areas requiring consideration of improvements would appear to be more definitive guidance for selecting assumptions, consideration of balance sheet accruals to include at least a minimum liability, and the required disclosures, including enterprise and affiliate securities held by pension funds and other transactions between such parties.

b. In the case of Japanese welfare pension plans (pension funds consist of a governmental social security portion and a private pension portion) and reserve for retirement allowances (Accrued liability for retirement allowances has been provided in the full or discounted present value of amount estimated to provide for indemnities to all employees if they retire on a voluntary basis. The difference between the prior period amount and the current period amount is accounted for as retirement cost.), one member country would like the IASC to consider an exemption from the application of IAS 19 and an acceptance of the treatment in Japan.

3. Suspense Issue

   a. Some IOSCO member countries may condition acceptance of the allowed alternative treatment of a projected benefit valuation method on disclosures providing information equivalent to the use of an accrued benefit valuation method.

4. Potential Long-Term Projects

   a. None.

H. IAS 21 (Revised 1993) The Effects of Changes in Foreign Exchange Rates

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

   a. The benchmark treatment of recognition of exchange differences as income or as expenses in the period they arise is acceptable, subject to suspense issues.

   b. Allowed alternative treatment - see suspense issue H.3.a. following.

   c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

   a. None.

3. Suspense Issues

   a. Some IOSCO member countries may condition acceptance of the allowed alternative treatment of recognition of certain exchange differences in the carrying amount of the related asset on disclosures providing information equivalent to the application of the benchmark treatment.

   b. Some IOSCO member countries may condition acceptance of the treatment allowed in paragraph 33(b) on disclosures providing information equivalent to the treatment allowed by paragraph 33(a).

   c. Consider foreign currency transaction hedging issues (see paragraph 2) in E48, Financial Instruments.

   d. The determination of the reporting currency and the manner of presentation of convenience translations of financial statements, both of which are not covered (paragraphs 4 and 5) by IAS 21 (revised 1993), would remain subject to host country regulations.

e. Some member countries may not require recognition of gains on long-term monetary items nor their disclosure in the footnotes.

f. One member country may not require recognition of gains or losses on long-term monetary items, but instead require disclosure in the footnotes.

4. Potential Long-Term Projects

a. None.

I. IAS 22 (Revised 1993) Business Combinations

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

a. The benchmark treatment of recognizing minority interests at the minority's proportion of the preacquisition carrying amounts of the net assets of the acquired entity is acceptable, subject to suspense issues. The benchmark treatment of recognizing negative goodwill by reducing the fair values of the non-monetary assets acquired proportionately and treating any excess that remains as deferred income is acceptable, subject to suspense issues.

b. The allowed alternative treatment of recognizing minority interests at the minority's proportion of the fair values of the net assets of the acquired entity is acceptable, subject to suspense issues. The allowed alternative treatment of recognizing negative goodwill as deferred income is acceptable, subject to suspense issues.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

a. None.

3. Suspense Issues

a. Some IOSCO member countries may condition acceptance of discounting to record acquired tax assets and liabilities (see the last sentence of paragraph 39) on disclosures providing information equivalent to recording tax assets and liabilities on an undiscounted basis. This matter could be considered further by the IASC in its project to revise IAS 12 on income taxes.

b. Consider the subsequent recognition of unrecognized acquired deferred tax assets in a revised standard on income taxes (see paragraph 69).

c. Consider eliminating alternatives for identifying and measuring impairment of the cost or carrying amount of goodwill in a project that also would consider long-lived assets and identifiable intangibles. Paragraphs 47 and 48 of the standard do not provide sufficient guidance to achieve reasonably comparable results in identifying impairment or for measuring impairment, e.g., should estimated future profits also cover interest costs for goodwill to be considered recoverable.

d. In reference to paragraph 13, consider the presentation of shareholders' equity and comparative financial statements following a reverse acquisition.

e. In reference to the last sentence of paragraph 3 and paragraph 8, consider new basis of accounting issues, including the following:

   (i) Push down accounting (including push down of debt);

   (ii) Promoter and related party transactions;

   (iii) Common control transactions (including downstream mergers and simultaneous transactions);

   (iv) Joint venture formations;

   (v) Master limited partnership formations;

   (vi) Leveraged buyouts;

   (vii) Mergers with unrelated shell corporations; and,

   (viii) Bankruptcies and reorganizations.

f. In reference to the last sentence of paragraph 6, consider requiring companies without subsidiaries to follow the same accounting for legal mergers as for companies with subsidiaries at least with respect to securities offerings and filings.

g. In reference to paragraph 8(b), consider limiting the scope exclusion for "interests in joint ventures and the financial statements of joint ventures" to joint venture formations.

h. In reference to paragraphs 49 to 51, some IOSCO member countries may accept recognition of negative goodwill in income in the year when a special cost, not recognizable as a result of the business combination, is expected to be incurred.

i. Some member countries have difficulty applying the accounting treatment for reverse acquisitions due to legal constraints.

j. One member country believes that in cases where the fair value of one enterprise or the scale of business is significantly greater than that of the other combining enterprise, if the shareholders of the combining enterprises share mutually in the risks and benefits of the combined entity, it should not be judged to be an acquisition and should be interpreted as a uniting of interests and the pooling of interest method should be allowed.

k. Some member countries have difficulty applying the accounting standard to legal mergers due to legal constraints.

4. Potential Long-Term Projects

a. Consider providing more definitive guidance on the bases for establishing provisions in connection with a business combination and more definitive guidance on the treatment of related costs of the acquiror and acquiree in connection with an acquisition.

J. IAS 23 (Revised 1993) Borrowing Costs

1. Evaluation of Required, Benchmark, and Allowed Alternative Treatments

a. The benchmark treatment of expense for all borrowing costs is acceptable.

b. Allowed alternative treatment - see suspense issue J.3.a. following.

c. Other required treatments, implementation guidance, and disclosures in the standard are acceptable, subject to suspense issues.

2. Essential Issues

a. None.

3. Suspense Issues

a. Some IOSCO member countries may condition acceptance of the allowed alternative treatment of capitalizing borrowing costs meeting certain specified criteria on disclosures providing information equivalent to the application of the benchmark treatment.

b. Some IOSCO member countries are prevented from capitalizing interest with respect to mere acquisitions.

4. Potential Long-Term Projects

a. None.

K. Impairment of the Cost of Assets

A suspense issue cited for IAS 16 (revised) and IAS 22 (revised) is the consideration of a project to eliminate alternatives for identifying and measuring impairment of the cost or carrying amount of certain assets. In considering the scope of such a project, the adequacy of guidance on impairment in other IASC standards and projects should be reviewed. This scope also possibly should include long-lived assets related to IAS 17 on leases and the current project on intangible assets.

L. Specialized Industries

A suspense issue cited for IAS 18 (revised) concerns revenue recognition issues and other specialized industry accounting and disclosure issues that may apply to various specified industries. In developing the IOSCO core standards, no attempt was made to consider the particular accounting issues related to specialized industries. To date, the IOSCO Accounting Subcommittee has attempted to identify industries that may require accounting and disclosure standards beyond the requirements of the core standards. The industries cited will need to be analyzed further before a decision can be made on the need or lack of a need for further guidance.

- End -