

## Summary note of the Accounting Standards Advisory Forum

held on 5 – 6 December 2013 at the IASB Offices Cannon Street, London

*This note is prepared by staff of the IASB, and is a high level summary of the discussion that took place. A full recording of the meeting is available on the IASB website.*

### ASAF members attending

Kim Bromfield	South African Financial Reporting Standards Council
Clement Chan	Asian-Oceanian Standard-Setters Group
Françoise Flores	European Financial Reporting Advisory Group
Russell Golden	Financial Accounting Standards Board (US)
Liu Guangzhong	Chinese Accounting Standards Committee
Liesel Knorr	Accounting Standards Committee of Germany
Roger Marshall	Financial Reporting Council (UK)
Ana Martinez-Pina	Instituto de Contabilidad y Auditoria de Cuentas (Spain)
Linda Mezon	Accounting Standards Board of Canada
Ikuo Nishikawa	Accounting Standards Board of Japan
Kevin Stevenson	Australian Accounting Standards Board

## Conceptual Framework

### Stewardship

1. ASAF members discussed a bulletin, published by EFRAG and the French, German, Italian and UK standard-setters, on accountability and the objective of financial reporting. The bulletin discussed three views on how stewardship or accountability should be addressed in the Conceptual Framework:
  - View 1: some think that the IASB has adequately addressed the importance and the role of accountability or stewardship in its *Conceptual Framework*;
  - View 2: some think that the provision of information on accountability or stewardship is the primary objective of financial reporting; and
  - View 3: some think that the provision of information on accountability or stewardship is a primary objective of financial reporting, not merely a part of, or ancillary to, another objective, and should be reinstated as such.
2. Some members of the ASAF supported View 1. Reasons expressed for supporting View 1 included:
  - The objective of financial reporting is, and should be, to provide information to users to help make economic decisions. Those decisions include decisions to buy, hold or sell equity and debt instruments, and decisions by those who have the right to vote on, or otherwise influence, management's actions.

- All, or most, information that is relevant for decisions to buy, hold or sell investments is also relevant for stewardship or accountability decisions.
  - Having two competing objectives could lead to unintended consequences.
  - Requiring information about management’s stewardship of the entity’s resources is the responsibility of the securities regulator. Emphasising stewardship as an objective could undermine the neutrality of the information provided to the users.
3. Other members of the ASAF supported View 3, because they believe that some important information that was needed to assess management’s stewardship (including disclosure about key management personnel compensation) would be omitted if the objective of financial reporting is to provide information that is useful in making decisions about providing resources to the entity. In particular, they argued that decisions about providing resources to an entity rely primarily on forward-looking information (information with predictive value), while stewardship or accountability decisions rely primarily on backward-looking information (information with confirmatory value). In their view, if providing information on stewardship is elevated to a primary objective, that would reduce the risk of omitting important information from financial statements.
  4. One ASAF member expressed the view that it is important not to confuse stewardship (management’s responsibility for the resources entrusted to it) with accountability (management’s responsibility to account for its stewardship of those resources).

## Reliability

5. ASAF members discussed a bulletin on reliability of financial information also published by EFRAG and the French, German, Italian and UK standard-setters. That bulletin considers whether the replacement of reliability with faithful representation, and the loss of the idea of the trade-off between relevance and reliability, is appropriate or whether there is an on-going need for such ideas in the Conceptual Framework. The bulletin recommends that the IASB should reinstate reliability (including verifiability) as a fundamental characteristic.
6. Some ASAF members supported the recommendation in the bulletin because they think that:
  - not having reliability as a fundamental qualitative characteristic could result in the recognition of assets or liabilities with highly uncertain measurements. Some saw this as a particularly significant concern in emerging economies, where there may be a lack of observable inputs to use in some measurements;
  - not having reliability as a fundamental qualitative characteristic could lead to the recognition of more intangible assets. Recognising more intangible assets does not have benefits that exceed the costs, because they believe that many users ignore the measurements attributed in financial statements to intangible assets; and
  - reinstating reliability would emphasise the need for the IASB to consider the trade-off between relevant and reliable information.

7. Other ASAF members support retaining faithful representation as a fundamental qualitative characteristic, instead of reinstating reliability. This is because they think that:
  - although the notion of faithful representation does not differ significantly from the notion of reliability, as it was defined in the IASB's 1989 Framework, many commentators used the term 'reliability' in a different sense. For example, commentators often used the term 'reliability' to refer to the degree of certainty about the ultimate outcome of a transaction, rather than to the degree of certainty about the measurement of the transaction;
  - if information gives a faithful representation of the economic phenomena, the users can rely on that information;
  - the Conceptual Framework already states that if the level of uncertainty in an estimate is too large, that estimate may not be particularly relevant. Consequently, there was no need to discuss a 'trade-off between relevance and reliability'. However some of these members suggested that it may be useful to better explain this relationship to minimise confusion among the stakeholders; and
  - it would not be productive to reopen the debate on this issue, which has already gone through extensive due process.
8. The IASB staff asked ASAF members who are considering recommending the reinstatement of reliability to explain clearly in their comment letters:
  - what they mean by reliability;
  - how it differs from the notion of faithful representation; and
  - what difference it would make to the decisions of the IASB when the IASB develops new Standards.

## Liabilities

9. ASAF members discussed a paper on liabilities published by the Australian Accounting Standards Board<sup>1</sup>. The discussion focused on the definition and recognition of liabilities and on differences between the approach proposed in the paper and the proposals in the IASB's Conceptual Framework Discussion Paper.
10. ASAF members discussed:
  - Whether the definition of liabilities should be restricted to enforceable obligations. Some ASAF members expressed a view that the definition of a liability should include only obligations that can be enforced by legal or equivalent means. They were concerned that the notion of a constructive obligation can be difficult to apply, and that including unenforceable obligations within the definition of a liability could give rise to recognition of costs that are not true obligations at the end of the reporting period.

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<sup>1</sup> AASB Occasional Paper No. 1 Liabilities – the neglected element: a conceptual analysis of the financial reporting of liabilities, Warren J McGregor, AASB Research Centre, October 2013

However, other ASAF members disagreed and stated that excluding obligations that will result in an outflow of economic resources would not be useful to the users of financial statements.

- Whether describing a liability as “an economic burden for which the entity is obligated” rather than a “present obligation” would help to identify when a liability arises. Some ASAF members thought that the “economic burden” wording was clearer and resulted in a liability definition that was symmetrical with the asset definition. However, others disagreed and questioned the need to separate the identification of a present obligation into two stages: the identification of an economic burden and the identification of a link between the economic burden and the entity that is obligated.
- Litigation liabilities and when they arise. The paper concludes that, conceptually, a litigation liability arises when an entity breaches a law. However, when developing particular Standards, the IASB may conclude, for cost-benefit reasons, that no liability should be recognised until the entity becomes aware of the breach.
- Obligations that are conditional on the reporting entity’s own actions (as discussed in paragraphs 3.72-3.97 of the IASB’s Discussion Paper). Some expressed the view that only strictly unconditional obligations should be treated as liabilities. Other ASAF members disagreed and stated that the objective of financial reporting (to provide useful information to users of financial statements) would require the identification of some liabilities before they became strictly unconditional. However, the challenge would be to identify when a conditional obligation gives rise to a liability.
- Recognition of liabilities. The paper states that, conceptually, items that meet the definition of liabilities are always relevant to users of financial statements and should be recognised (that is, at a conceptual level there should be no recognition criteria). However, when developing particular Standards, the IASB might decide that the costs associated with recognition outweigh the benefits. Some ASAF members disagreed with this conclusion, arguing that including recognition criteria in the Conceptual Framework would help the IASB to develop consistent standards.

### **Profit or loss, other comprehensive income (OCI) and measurement**

11. ASAF members discussed a paper prepared by the Accounting Standards Board of Japan (ASBJ) that:
  - proposes definitions of comprehensive income, profit or loss and OCI;
  - identifies when two measurement bases could be used for the same item; and
  - proposes an approach to recycling.
12. ASAF members welcomed the ASBJ’s paper. It was noted that many stakeholders have asked the IASB to define profit or loss, but the ASBJ is the first organisation to develop a definition.

13. ASAF members discussed:

- whether comprehensive income, profit or loss and OCI should be defined. Some ASAF members supported the ASBJ's approach of defining these items. However, one IASB member thought that a precise definition of profit or loss or OCI may not be possible and, consequently, the issue of what should be reported in profit or loss and OCI should be dealt with through presentation.
- the proposal in the paper that profit or loss should be described as an all-inclusive measure of irreversible outcomes of an entity's business activities in a certain period:
  - Some ASAF members asked the ASBJ to clarify what is meant by the term 'irreversible'. For example, how does the irreversibility concept apply to impairments and changes in estimates of long-term liabilities? Some ASAF members stated that they have concerns about whether the concept of irreversibility could be made to work.
  - Some ASAF members stated that the approach proposed in the ASBJ's paper was less complex than the approach proposed in the IASB's Discussion Paper. However, it would need more work to identify the consequences of the proposed approach.
  - Some ASAF members suggested that consideration of an entity's business model may help to identify the measure that should be reported in profit or loss.
- recycling: some ASAF members agreed with the ASBJ's proposal that all items reported in OCI should be recycled (ie as an automatic consequence of the measure reporting in profit or loss). However, other ASAF members stated that they disagreed with recycling because it may allow for earnings management.
- measurement and how it relates to the definition of profit or loss and financial performance:
  - Most ASAF members stated that it is important that measurement and the reporting of financial performance should be considered together, because they affect each other.
  - An ASAF member supported the way in which the ASBJ paper closely connected the choice of measure(s) to represent financial position and measures to report financial performance (with OCI as the link). He suggested that this aspect of the proposals could be explored further, particularly on how the different inputs used to measure an item could help to decide what should be reported in OCI (and whether it should be subsequently recycled).
- whether the statement of comprehensive income should be split between profit or loss and OCI. Some ASAF members stated that they would prefer a single statement of comprehensive income. They argued that the existing split between OCI and profit or loss over-simplifies the reporting of financial performance. However, others noted that

profit or loss is an important number and is considered by many users to be the primary indicator of an entity's financial performance.

## **Post-implementation Review (PiR)—IFRS 3 *Business Combinations***

14. It was explained that the purpose of this agenda item was to gather ASAF members' input on the work that it is being undertaken on the Post-implementation Review (PiR) of IFRS 3 *Business Combinations*. Members were asked to provide feedback on areas already identified as being challenging in implementing the Standard and on a suggested set of questions that had been proposed for inclusion in the Request for Information ('the RfI'), Agenda Paper 5B.
15. An ASAF member asked how important the work completed by the Financial Accounting Foundation (FAF) on the post-implementation review of SFAS 141R<sup>2</sup> and fair value had been on influencing the work for this PiR. It was explained that the scope of the FAF and IASB reviews are different. FAF considered only SFAS 141R and therefore it did not consider the accounting for goodwill, whereas the IASB review includes accounting for goodwill. Consequently, there are differences in scope, which may give rise to different issues.
16. An ASAF member noted that SFAS 141R and IFRS 3 were developed as a joint project between the FASB and IASB with considerable effort in made to achieve a converged solution - the PiR should not disregard this.
17. The FASB representative noted the questions in Paper 5B seemed appropriate and that the FASB has considered some of the FAF's recommendations but is waiting for the IASB to reach its conclusion on the PiR of IFRS 3 before devoting resources to the project.
18. It was, however, noted that the FASB had endorsed the Private Company Council decision to amortise goodwill and it was undertaking research to evaluate whether this treatment could be extended to public companies in the United States. Further, the FASB has just announced a review of SFAS 160 *Noncontrolling Interests in Consolidated Financial Statements*, which is within the scope of the PiR of IFRS 3.
19. An ASAF member noted that the non-amortisation of goodwill and intangible assets with indefinite useful lives was a controversial topic within the Business Combinations project. It was recommended that the question in the RfI should be clarified to invite specific comments on whether non-amortisation is appropriate. It was also suggested that the research project on goodwill amortisation (currently being undertaken by the standard-setters of Japan, Italy, India and EFRAG) could provide useful input to the PiR.
20. A further ASAF member noted that the recognition of full goodwill was also very topical in the Business Combinations project. It would be interesting to do some research on who has chosen to use partial goodwill and who has chosen full goodwill.
21. There was a further discussion in which ASAF members outlined a large number of other potential items that might be included in the RfI. IASB staff noted that it is important to manage expectations and they warned that including too many items in the RfI might raise undue expectations. In addition, some items raised may fall outside the scope of the PiR, such

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<sup>2</sup> FASB Statement No. 141, *Business Combinations*

as the fair value measurement. It was suggested that items raised but outside the scope should be included in the Feedback Statement, which should be as comprehensive as possible in reporting the input received.

22. Ian Mackintosh, IASB Vice-Chair, reflected that we should ask what the object of PiRs is and what the expected outcome might be. An ASAF member noted that PiRs should also be undertaken for “old Standards”. Hans Hoogervorst, IASB Chair, stated that the objective should be that for “recent Standards” you are only looking for unintended consequences and evidence of practical problems, rather than for a fundamental review of the core of the Standard.

## Leases

23. IASB staff presented a paper that summarises the feedback received on the 2013 *Leases* ED, providing a high level overview of the feedback on the lessee model, the lessor model and other aspects of the proposals. IASB members and staff also explained the next steps on the project—the IASB and the FASB would start to discuss the lessee model, the lessor model and any possible scope simplifications in January 2014, with the aim of reaching decisions on those central topics in March 2014. The staff are currently analysing the costs and benefits of various possible paths forward—the main difficulty for the boards and staff is the range of differing views received in the feedback.
24. ASAF members asked how they could help with those next steps. IASB members and staff indicated that they would hope to obtain ASAF members’ views on the costs and benefits of the various possible paths forward at the next ASAF meeting and, in the meantime, would be available for individual meetings with ASAF members by video.

## Rate-regulated Activities

25. The aim of this agenda item was to obtain feedback from the ASAF members on the staff’s preliminary analysis and how this could be developed further for inclusion in the Discussion Paper on Rate-regulated Activities.
26. IASB staff presented a summary of the common features of rate regulation being considered in the preliminary analysis. No accounting model was discussed, because the project is still in its research phase and no decisions had yet been made by the IASB on whether the rate-setting mechanism described does give rise to assets and liabilities. The staff clarified that the objective was to publish a Discussion Paper in 2014.
27. ASAF discussed the scope of the project and the IASB staff’s preliminary analysis of whether a rate-setting mechanism that incorporates a particular type of adjustment feature could result in the existence of assets and liabilities. The preliminary analysis applies the proposed definitions of assets and liabilities and the related guidance material contained in the Discussion Paper: *A Review of the Conceptual Framework for Financial Reporting*, published in July 2013.
28. The ASAF members agreed that defining the scope of the preliminary analysis and any accounting model that was being developed was critical to the project and asked for some clarifications. ASAF members questioned whether the features identified as being those that

distinguish rate-regulated activities from other commercial activities were sufficient. It was suggested that the analysis should consider which features represented similarities with other commercial activities as well as which features represented differences.

29. Although some ASAF members expressed the view that specific rights or obligations contained in the rate regulation might, in limited circumstances, give rise to assets or liabilities, many expressed scepticism about the feasibility of developing a model that could be widely applied. Some ASAF members suggested that the analysis should focus more on whether the rate regulation created an 'opportunity' to earn revenue and that it might be appropriate to account for this 'opportunity' as an intangible asset.
30. An ASAF member questioned if recognition of regulatory assets and liabilities should be considered symmetrically, and noted that the need of symmetry should be discussed in the project to review the Conceptual Framework.
31. Some ASAF members suggested that the analysis should focus more on revenue recognition or performance and should consider the issue from an income statement perspective. The outcome of that analysis should then be compared against the proposals being developed in the Conceptual Framework project, including the definitions of 'asset' and 'liability'.

## General project update

32. The IASB staff highlighted the following items:
  - Because of the stage of development of IFRS 9, there are currently no plans to discuss this Standard with ASAF again.
  - Progress is being made on the Disclosure Initiative project, including:
    - Merger of the technical team and the XBRL team. The aim of the merger is to improve the relationship between the taxonomy team and the technical team, so that in the longer term it will be easier for investors to consume information and also to ease preparation of electronic data for the preparers.
    - The proposals to amend IAS 1 will be issued in 2014, the aim being to remove impediments to good financial reporting.
    - There is a small working group considering the application of materiality. This is a complex issue but the IASB is trying to find ways of improving the application of materiality.
    - A broader project is looking at IAS 1, IAS 7 and IAS 8.
  - A cautious start to the research projects has been made:
    - The Business Combinations under Common Control work has begun, with the IASB starting by looking at particular transactions.
    - A first paper on the discount rate will be presented to the IASB in early 2014.

- The equity method project will be considered in 2014 – the need to commence work on this topic is highlighted by the number of implementation issues that are arising in this topic.
33. An ASAF member asked if IAS 37 and IAS 20 were being considered as part of the research agenda. There was no project to look at IAS 20, but there was a link with the Rate-regulated Activities project. Any issues concerning IAS 37 really relate to the Conceptual Framework project.
  34. FASB noted that it would be happy to present a summary at the March 2014 ASAF meeting of the feedback to the work it is undertaking in relation to disclosures. FASB have been undertaking fieldwork on how an entity can improve its disclosures.
  35. One ASAF member noted that research projects are good topics for discussion at ASAF. A report on the activities of members could stimulate discussion and participation among members and might lead to greater sharing of research work among ASAF members.

### **Forward agenda**

36. The proposals for future agenda items were discussed, and no comments were raised.
37. A general paper regarding the causes of complexity in standard-setting, which is being written by EFRAG and the French, German, Italian and UK standard-setters, could be presented at the next meeting. The paper does not directly address a specific topic in the Conceptual Framework Discussion Paper but address wider causes of complexity relevant to both the Framework and individual standards.