Summary note of the Accounting Standards Advisory Forum

Held on 6 and 7 December 2018 at the IFRS Foundation office, Columbus Building, 7 Westferry Circus, Canary Wharf, London E14 4HD.

This note is prepared by staff of the International Accounting Standards Board (the Board), and summarises the discussion that took place with the Accounting Standards Advisory Forum (ASAF).[1] A full recording of the meeting is available on the IFRS Foundation® website.

ASAF members and specialists attending

Africa	
Pan African Federation of Accountants (PAFA)	Raymond Chamboko
Asia-Oceania	
Asian-Oceanian Standard Setters Group (AOSSG)	Shiwaji Bhikaji Zaware
	Christina Ng
	Il-Hong Park
	Kris Peach
Accounting Standards Board of Japan (ASBJ)	Yukio Ono
	Atsushi Kogasaka
	Yasunobu Kawanishi
Accounting Regulatory Department, Ministry of Finance PRC (ARD)	Yu Chen
	Yun Huang
Korea Accounting Standards Board (KASB)	Eui-Hyung Kim
	Sungsoo Kwon
	Won-Hee Han
Europe	
European Financial Reporting Advisory Group (EFRAG)	Andrew Watchman
	Patricia McBride
Autorité des normes comptables (ANC)	Patrick de Cambourg
	Cédric Tonnerre
Organismo Italiano di Contabilità (OIC)	Alberto Giussani
	Tommaso Fabi
	Leonardo Piombino
Financial Reporting Council (FRC)	Paul George
	Anthony Appleton
The Americas	
Group of Latin American Standard Setters (GLASS)	Alexsandro Broedel
	Rodrigo Morais
Canadian Accounting Standards Board (AcSB)	Linda Mezon
	Lester Cheng
	Katharine Christopoulos
Financial Accounting Standards Board (FASB)	Russ Golden
	Jim Kroeker

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Financial Instruments with Characteristics of Equity

1. Following on from the preliminary views discussed at the October 2018 ASAF meeting, the objective of this session was for the ASAF members to provide comments on the Discussion Paper *Financial Instruments with Characteristics of Equity* (Discussion Paper) based on the outreach in their jurisdictions.

2. The EFRAG member provided an overview of EFRAG's outreach activities and a summary of feedback received. The following comments were highlighted by the EFRAG member.

Comments on classification proposals

3. Acknowledgment of the potential advantages of the proposals in the Discussion Paper that:

   (a) clearer classification principles would provide a better basis for developing more detailed application guidance and determining classification of innovative financial instruments as they emerge; and

   (b) users of financial statements acknowledge that there is room for improvement in IAS 32 *Financial Instruments: Presentation* and are interested in having an approach that distinguishes between claims that depend on the entity's available economic resources and those which are independent of such resources.

4. Concerns that:

   (a) the cost of applying classification proposals set out in the Discussion Paper including the cost of reassessing classification decisions on existing financial instruments may outweigh the benefits. This concern stems from the new terminology introduced in the Discussion Paper;

   (b) potential new interpretive issues may arise;

   (c) the clarity of the 'amount' and 'timing' features needs improvement, including aspects of the 'amount' feature, such as 'available economic resources'; and

(d) the potential change in the classification from equity to financial liabilities of cumulative preference shares and some hybrid bonds[2] could disrupt their market.

5. The EFRAG member noted that some stakeholders have suggested addressing practice issues by issuing application guidance rather than classification proposals (ie the 'amount' and the 'timing' feature).

6. He also said some resistance had been expressed to the proposal that takes into consideration what happens on liquidation when classifying a financial instrument because of the view that this is inconsistent with the going concern assumption.

Comments on presentation proposals

7. The EFRAG member reported mixed views expressed by stakeholders on the Discussion Paper's proposal to present income and expenses arising from particular financial liabilities within other comprehensive income (OCI) without recycling. Some stakeholders who support this proposal note that the challenge remains on determining the appropriate scope of the financial liabilities to which such approach should apply.

8. He also noted a lack of support for the presentation proposal in relation to attribution of total comprehensive income to equity instruments. Complexity and cost of preparation was reported as the main concern.

Comments on disclosure proposals

9. The EFRAG member noted that, generally, more support had been received for the disclosure proposals compared to other parts of the Discussion Paper. He noted that:

   (a) questions had been raised on the interaction of the disclosure proposals in Discussion Paper with the Board's *Principles of Disclosure* project;

   (b) challenges had been acknowledged regarding providing a sufficient amount of information on terms and conditions of financial instruments whilst avoiding disclosure overload;

[2] The EFRAG member said that the European hybrid bonds market in 2018 represents about 5% of the total market for new issuance of bonds and approximately EUR 20 billion in Euro market.

(c) challenges acknowledged regarding the proposed disclosure of the priority of claims on liquidation on a consolidated basis; and

(d) questions had been raised on the interaction between the accounting within equity of put options written on non-controlling interests (NCI puts) as set out in the Discussion Paper and the requirements in IFRS 10 *Consolidated Financial Statements*.

10. In response to the EFRAG member comments the IASB Vice-chair encouraged ASAF members to consider the following in responding to the Discussion Paper:

(a) How the approach proposed in the Discussion Paper will contribute to better financial reporting in the longer term. She noted that the Board can consider developing transition arrangements to address concerns on the costs of applying the Board's preferred approach.

(b) To be specific about which part of the proposals the stakeholders support and which parts they have concerns over, for example, in relation to concerns about the 'amount' feature, it would be beneficial for the comment letters to:

(i) distinguish whether the concerns exist over the focus on what would happen on liquidation or the concerns are broader.

(ii) specify whether the concerns exist with respect to the notion of the 'amount' feature itself or whether the concerns relate to the clarity of the articulation.

(iii) provide suggestions on the best approach to address concerns associated with the existing notion of 'fixed-for-fixed' applied to derivative financial instruments should they not agree with the amount feature.

(iv) understand whether investors share the same concern raised over the classification outcome for cumulative preference shares.

(c) Acknowledging the challenges in providing information on priority of claims on liquidation in the consolidated financial statements, it would be beneficial to understand how challenges may have been overcome when providing similar information, for example, the Board's understanding is that such information is already required to be provided in some securities offering documents in a particular jurisdiction.

(d) Outreach activities have revealed a significant level of diversity in the application of IAS 32, for example, the application of the ‘fixed-for-fixed’ condition. Consequently, it would be useful to receive suggestions on how to address the current diversity in practice.

11. The GLASS member asked whether the change in classification for financial instruments such as cumulative preference shares represents an intended consequence. Whilst he agreed the change in classification for such financial instruments reflected the economic substance and that many stakeholders already regard them as financial liabilities, he noted such change is likely to be disruptive especially due to its implication for financial covenants.

12. The Board member responded that this was an intended consequence. She highlighted that these types of financial instruments behave like debt and are often regarded as such by various parties. Another Board member noted she had received feedback that at least one of the rating agencies treat these types of financial instruments as fifty percent equity and fifty percent debt, independently of their accounting classification.

13. The ARD member highlighted the importance of this project for China and noted the prevalence of perpetual bonds in its market. The member said that comments raised by stakeholders in China were similar to those presented by the EFRAG member set out above. In addition to the comments made by the EFRAG member she highlighted the following matters which have been raised:

(a) constituents urge the Board focus on addressing practice issues rather than introducing new terminology;

(b) how regulatory and legal requirements should be considered when applying the Board’s preferred approach; and

(c) additional guidance is needed as how to consider economic compulsion and indirect obligations when determining whether rights and obligations arise from the contractual terms.

14. The AcSB member updated ASAF members on the outreach events conducted in her jurisdiction, highlighting the balanced and widespread range of stakeholders involved

in their outreach programme. She also noted that the comments raised were similar to those presented by the EFRAG member. In addition to the EFRAG member's comments she noted:

(a) agreement with discussions regarding the change in classification of cumulative preference shares, however she highlighted the implications of such a change on the regulatory capital treatment;

(b) questions about the interaction of the definition of financial liabilities in the Discussion Paper with the *Conceptual Framework for Financial Reporting* and IFRS 2 *Share-based Payments*;

(c) support expressed by users of financial statements for the proposed disclosures on terms and conditions of financial instruments and priority of claims; and

(d) that some users argue that the proposals in the Discussion Paper would (if implemented) expand the use of OCI which in turn lacks a conceptual definition. However, these stakeholders agree that presenting gains and losses from particular types of financial instruments separately from profit and loss represents their characteristics more faithfully.

15. The FRC member noted that he agreed with many of the earlier comments raised by other members. However, he thought that in hindsight it would have been more useful for the Discussion Paper to fundamentally review the key principles of IAS 32 rather than focusing on specific areas.

16. The OIC member said they are generally supportive of the main principles underpinning the Discussion Paper but consider more guidance is needed for compound financial instruments, particularly the accounting for NCI puts in the separate financial statements. In addition to comments made by previous ASAF members, he made the following comments:

(a) the Board should undertake an effect analysis considering the risk of unintended consequences resulting from the introduction of the new concepts;

(b) a preference for subsequent recycling from OCI to profit and loss for income and expenses arising from particular financial liabilities;

(c) the need for an accounting definition of liquidation in the context of Discussion Paper;

(d) support for the proposal for disclosure on maximum dilution of ordinary shares while not supporting the presentation proposal for the attribution within equity; and

(e) strong support for the proposal for retaining the puttable exception.

17. The ASBJ member said that constituents in Japan, in particular users of financial statements, are generally supportive of the proposals in the Discussion Paper and welcome the disclosure proposals, especially disclosures on maximum dilution and priority of claims on liquidation. The following additional comments were made by the ASBJ member:

(a) the Board should proceed with proposed improvements to disclosures even if it decided not to proceed with the classification proposals; and

(b) some of the application issues with IAS 32 arise not because of unclear principles but rather due to confusion as to what unit of account such principles apply to.

18. The AOSSG member noted that the comments made by the EFRAG member resonated with the feedback from constituents in her region and highlighted, in addition to comments made by members, that the proposal in the Discussion Paper to remove the foreign currency exception lacks rationale and is inconsistent with approach taken to retain the puttable exception.

19. The same member noted that despite the general concerns, stakeholders acknowledge the issues arising with IAS 32 and think more problems will arise in the future if not addressed now.

20. The ANC member said that constituents in France welcome the initiative to tackle existing known problems with IAS 32, including those that often lead to structuring opportunities. They are supportive of the disclosure proposals while they do not support presentation proposal for attribution within equity. The member highlighted practical challenges that relate to the application of indirect obligation and economic compulsion and encouraged the Board to explore further how to address this issue.

21. The KASB member said that they share similar views to those already highlighted by ASAF members. In addition to comments already made by members, he said that auditors and those that are familiar with IAS 32 welcomed the clearer principles and articulation provided by the 'timing' and 'amount' features. That is because the amount feature addresses the challenges associated with 'fixed-for-fixed' condition and because it is more intuitive to classify a claim as financial liability if it contains an obligation to deliver a fixed amount of cash or another financial asset regardless of the timing feature.

22. With regards to proposals for presentation in OCI, the KASB member said there are mixed views with some considering that the qualifying criteria are difficult to apply, for example, partly independent derivatives, whilst others argue the contrary given only limited number of financial instruments qualify for such presentation. Constituents in his jurisdiction considered the attribution of OCI within equity as too costly to apply.

23. The KASB member also noted that local stakeholders expressed concerns over the classification outcomes applying the Board's preferred approach for two types of financial instruments: a hybrid instrument prevalent in Korea which would change its classification to a financial liability and a bond with warrant containing anti-dilution provisions which would remain classified as a financial liability.

24. The FASB member explained the practical challenges associated with financial instruments that are indexed to and settled in equity, and said that the FASB has an ongoing project that shares similar philosophy with the FICE project in some aspects. The feedback gathered so far as part of the project indicates that investors do not support bifurcation of hybrid financial instruments but instead prefer more disclosures about the terms of these financial instruments and their ranking in the waterfall.

25. A Board member emphasised that it would be very helpful if ASAF members' comment letters could segregate the comments each had received by stakeholder types.

Business Combinations Under Common Control (BCUCC)

26. The objective of this session was to seek ASAF members' views on whether a current value measurement approach based on the acquisition method set out in IFRS 3 *Business Combinations* should be applied to all or some BCUCC that affect non-controlling shareholders in the receiving entity and if not, how the distinction should be made on when to use a current value measurement approach. In particular, the staff sought views on whether the nature of non-controlling interest (NCI) (for example, whether NCI is present in a receiving entity whose equity instruments are traded in a public market), the size of the NCI or both factors should be considered in deciding when a current value measurement approach should be required.

27. Half of the ASAF members (EFRAG, OIC, ANC, FRC, GLASS and AcSB) supported a current value approach when NCI is present in the receiving entity. In addition, some of those members thought that a current value approach should not be restricted to when the receiving entity's equity instruments are traded in a public market. However, the members acknowledged distinguishing when to use a current value approach for private entities when NCI is present would be difficult.

28. In addition to the discussion in the agenda paper of the nature or size of the NCI as possible way to distinguish when to use a current value approach in BCUCC, some ASAF members suggested alternative ways of making the distinction:

    (a) Three members (AOSSG, FRC and EFRAG), discussed whether the NCI in the receiving entity should be asked whether they want current value information, similar to the exemption from producing consolidated financial statements in IFRS 10. One ASAF member (OIC) expressed a view that such an approach would be operationally challenging in practice.

    (b) The FASB member suggested leaving the decision about using a current value approach to the entity's management.

    (c) The AOSSG member suggested considering the notion of 'public accountability' as described in the *IFRS for SMEs* Standard.

29. Some ASAF members supported using a current value approach for BCUCC in some situations but suggested the following alternative ways of approaching the problem instead of focussing on the information needs of primary users of the receiving entity's financial statements:

(a) Consider commercial substance of a BCUCC in determining the appropriate measurement approach (ie if the BCUCC has the same substance as a business combination as defined applying IFRS 3, then AOSSG members, except for ARD, consider that a current value approach can provide useful information about the transaction; if the substance of the BCUCC is different from a business combination then a different approach might be appropriate.).

(b) Consider whether the transaction is an acquisition or a reorganisation (PAFA). However, the member did not suggest how to make such a distinction.

(c) Start the problem analysis considering BCUCC between wholly-owned entities instead of considering transactions where NCI in the receiving entity is affected (ASBJ).

(d) Develop general principles for BCUCC before considering specific examples (KASB).

30. The AOSSG considered information needs and cost-benefit analysis for different primary users (such as NCI and the controlling party) are generally different, and so it would be challenging to determine the measurement basis for BCUCC by focusing on a particular type of primary users of financial reports without compromising the information needs or cost-benefit considerations for other types of primary users.

31. The ARD member did not agree with the use of a current value approach for transactions within the scope of the project. Instead, the member advocated the use of a predecessor method and noted that a predecessor method is currently used in the member's jurisdiction.

32. The AcSB and EFRAG members questioned the focus on structuring considerations in the staff's analysis. They noted they had not seen structuring transactions in practice by creating or changing NCI. The PAFA member expressed a view that regardless of the approach taken in the project, it should not allow creation of values artificially.

Pension Benefits that Depend on Asset Returns

33. The objective of this session was to obtain ASAF members' advice on whether the measurement approach described in Agenda Paper 7 would be helpful in solving the measurement inconsistency described in that paper when applying IAS 19 *Employee Benefits* to pension benefits that depend on asset returns.

34. Most ASAF members (EFRAG, KASB, ANC, FRC, AcSB, FASB and ARD) expressed support for the research project and the proposal to address the specified measurement inconsistency.

35. The EFRAG member said that he agreed with the proposal to keep the project scope narrow. He also mentioned that EFRAG is conducting its own pension research project on pension plans with a return-based promise and is planning to publish a discussion paper in the first quarter of 2019. The EFRAG member said that the EFRAG project considers both the approach being explored by the Board and other approaches - a fair value approach and a fulfilment value approach.

36. The EFRAG member suggested the IASB staff consider the impact of any 'backloading' features on the approach being explored by the Board. He also suggested the staff explore interactions with benefits that include guarantees (ie when the employee is guaranteed the 'higher of' two or more possible outcomes, of which one is based on the actual return on plan assets). The staff said that they intend to explore interactions with guarantees, to assess whether any unintended consequences would arise if the approach being explored by the Board were applied without also addressing 'higher of' guarantees.

37. The AOSSG member asked some questions around the scope of the project but said that, given the nature of benefit arrangements in their region, the issue under discussion was not particularly prevalent.

38. A few ASAF members (KASB, ANC and AOSSG) questioned whether the approach being explored would be appropriate in situations where the assets are not held, or controlled by, the entity providing the benefit that is dependent on the return on those assets. The staff explained that the measurement inconsistency arises within the measurement of the liability (the defined benefit obligation) due to the use of different estimates in the measurement of the liability – the assumed rate of return used to estimate the cost of asset-dependent pension benefits reflects the return investors

expect for bearing the risk associated with the underlying assets, but the discount rate used to discount those pension benefits to their present value does not reflect those risks. The staff said that this measurement inconsistency arises regardless of whether the specified assets are actually held by the entity. However, the staff agreed that the inconsistency is more visible if an entity holds the asset.

39. The FRC member although supporting the approach, said that it may be challenging to keep the project scope narrow. The staff responded that because the approach being explored by the Board focuses only on estimating cash flows for benefits that vary with asset returns, the scope of the approach is self-defining.

40. The ANC and ARD members suggested that the measurement inconsistency might be addressed by adjusting the discount rate instead of adjusting the estimated cash flows. The EFRAG member said that such an approach would be less viable than the approach that the Board is exploring. This is because the pension benefits provided to an employee may be a composite of both a benefit that depends on asset returns and other forms of benefits. Accordingly, such an approach would mean applying different discount rates to different cash flow streams within the overall benefit arrangement. The staff said that adjusting the discount rate would require the Board to define the scope of that adjustment because it would not be self-defining.

41. The ARD member was appreciative of the efforts by the Board to try and solve the measurement inconsistency but also expressed some concerns about the approach that the Board is exploring. She said that some stakeholders in her region thought that the discount rate and expected rate of return on assets were two separate and distinct assumptions and addressed two different concepts in IAS 19. She also suggested that users of financial statements might be confused if, in applying the capped rate to pension benefits that vary with asset returns, two entities used the same estimates of the rate of return on different assets subject to different risks. Thus, she suggested applying an approach similar to the approach described in paragraph 17 of Agenda Paper 7 where, applying paragraph 115 of IAS 19, the fair value of qualifying insurance policies that exactly match the amount and timing of some or all of the benefits payable under the plan is deemed to be equal to the present value of the defined benefit obligation.

42. The FASB member said that a similar inconsistency arises in their jurisdiction where the discount rate and the expected rate of return are set at different levels for cash-balance pension arrangements. He also said that the FASB has explored this measurement inconsistency but has not been successful in finding an appropriate solution. The FASB member commended the efforts of the Board in exploring this matter and offered to provide access to their past research work on similar issues to the staff.

43. The AcSB member said that she was supportive of what the Board is trying to achieve and offered to share the research findings (from a research project on pension that they are undertaking with other national standard-setters) with the staff to help support the research activities for this project.

IFRS 17 *Insurance Contracts*

44. The objective of this session was to ask ASAF members' advice on six topics in IFRS 17 *Insurance Contracts* that the Board is considering for possible amendments to the Standard. The staff presented Agenda Paper 4.

Scope of IFRS 17 – Loans and other forms of credit that transfer insurance risk

45. Some ASAF members (KASB, FRC, ARD, ANC) welcomed that the staff are analysing possible amendments to IFRS 17 to exclude from its scope some or part of insurance contracts that have as their primary purpose the provision of loans or other forms of credit in a way that would meet the criteria set by the Board. Those ASAF members provided the following comments for this topic:

    (a) the KASB member proposed allowing an entity to choose to apply either IFRS 17 or IFRS 9 *Financial Instruments* to account for those contracts and that the entity should be required to apply that choice consistently.

    (b) the FRC member agreed that accounting for some insurance contracts applying IFRS 9 might provide relevant information. He observed that amending the requirements in IFRS 17 about the separation of non-insurance components from an insurance contract would be more complex then amending the requirements in IFRS 17 to exclude some additional insurance contracts from the scope of the Standard.

(c) the ARD member noted that if the Board were to propose any amendments to the scope of IFRS 17, consequential amendments to other Standards might be necessary.

(d) the ANC member expressed the view that a review of the interaction between IFRS 17 and IFRS 9 is needed when possible amendments to IFRS 17 are finalised.

46. The AcSB member observed that it would be difficult to amend IFRS 17 to exclude some additional insurance contracts from the scope of the Standard. Therefore, stakeholders in her jurisdictions do not think that the Board could amend the scope of IFRS 17 without unduly disrupting implementation processes that are already under way.

Acquisition cash flows for renewals outside the contract boundary

47. Some ASAF members (KASB, ANC, AcSB, FRC) agreed with the staff preliminary views that it might be possible to amend IFRS 17 to require or allow an entity to allocate insurance acquisition cash flows directly attributable to a contract not just to that contract, but also to expected renewals of that contract in a way that would meet the criteria set by the Board. The AcSB member observed that an approach that would result in an entity recognising an asset for deferred acquisition costs might require the entity to perform an impairment test on that asset.

48. In contrast, the ARD member expressed concerns about possible amendments to IFRS 17 requirements about acquisition cash flows. She noted that:

(a) deferring acquisition cash flows for renewals is not common in her jurisdiction—the local insurance regulator does not encourage such accounting approach; and

(b) it is difficult in practice to distinguish the acquisition costs that pertain to the original insurance contract from those that pertain to a renewed insurance contract.

Contractual service margin: coverage units in the general model

49. Most ASAF members (KASB, ANC, AcSB, FRC, ASBJ, ARD, AOSSG) welcomed the staff exploring possible amendments to IFRS 17 for the determination of coverage

units of insurance contracts to which the general model applies (general model contracts).

50. Some of those ASAF members (KASB, AcSB, FRC, ARD, AOSSG) noted that some stakeholders in their jurisdictions think that the allocation of the contractual service margin for general model contracts should reflect both the insurance coverage and the investment-related services provided by the contracts or the existence of an investment component in the contracts. Two ASAF members (AcSB and FRC) mentioned annuities as an example of contracts for which such allocation would be relevant.

51. The KASB member also noted that amending the requirements about coverage units for general model contracts might have a pervasive effect on IFRS 17 and agreed that the Board should consider only amendments that would not unduly disrupt implementation processes that are already under way.

52. The AOSSG member also noted that some stakeholders in Hong Kong support maintaining a distinction between general model contracts and variable fee contracts. Those stakeholders would welcome a revision of the requirements for the allocation of the contractual service margin for general model contracts using a principle-based approach.

Reinsurance contracts held: initial recognition when underlying insurance contracts are onerous

53. Half of the ASAF members (KASB, ANC, AcSB, FRC, ARD, AOSSG) agreed the Board should explore possible amendments to IFRS 17 about the initial recognition of reinsurance contracts held when the underlying groups of insurance contracts is onerous in a way that would meet the criteria set by the Board.

54. Three ASAF members (AcSB, FRC, AOSSG) noted that some stakeholders have already submitted suggestions for the Board to consider in this respect, including two alternative approaches referred to as ‘balance sheet approach’ and ‘profit or loss approach’. The ARD member suggested that the Board should consider an approach similar to the risk mitigation exception in paragraphs B115–B118 of IFRS 17 for reinsurance contracts held.

55. Two ASAF members (ANC and AOSSG) suggested that the Board should explore possible solutions to address other concerns and implementation challenges raised by

stakeholders about the measurement of reinsurance contracts held, notably the ineligibility of reinsurance contracts for the variable fee approach (ANC) and the expected cash flows arising from underlying insurance contracts not yet issued (ANC and AOSSG).

Separate presentation of groups of assets and groups of liabilities

56. Half of the ASAF members (KASB, ANC, AcSB, FRC, ARD, AOSSG) agreed with the staff recommendation for the December 2018 Board meeting that, for cost-benefit reasons, the Board should consider amending in IFRS 17 for the presentation of insurance contracts on the statement of financial position to require entities to present portfolios of assets separately from portfolios of liabilities (rather than groups of assets separately from groups of liabilities). However, the ANC member said that the main concerns expressed by stakeholders is about retaining the level of information that is currently available in the statement of financial position of insurance entities, rather than the level of aggregation used in IFRS 17 for the presentation of insurance contracts.

57. Two ASAF members (KASB and ARD) acknowledged that the existing requirements in IFRS 17 are consistent with the *Conceptual Framework for Financial Reporting* and are concerned that offsetting assets and liabilities might result in loss of useful information.

Transition – Modified retrospective approach: further modifications

58. A few ASAF members (KASB, AcSB, FRC, ARD) agreed with the staff preliminary thoughts that it might be possible to amend IFRS 17 for the modified retrospective approach by introducing additional modifications in a way that would meet the criteria set by the Board. Possible simplifications mentioned by those ASAF members include justifications that an entity should be able to use the modified retrospective approach (rather than the fair value approach), the calculation of discount rates, the use of historical cash flows and the retrospective application of the requirements for interim financial reports.

Other comments

59. Most ASAF members appreciate the work the Board is undertaking to respond to the concerns and implementation challenges raised by stakeholders since the issuance of

the Standard. Two ASAF members (ANC and FRC) expressed the view that Board should focus on amendments that would improve financial information for insurance contracts, rather than on amendments that would limit disruption to implementation processes under way.

60. The ANC member mentioned that the ANC has already submitted suggestions for the Board to consider when responding to the concerns and implementation challenges raised by stakeholders regarding the level of aggregation, acquisition cash flows for renewals outside the contract boundary and the separate presentation of groups of assets and groups of liabilities. The ANC plans to submit its suggestions regarding the accounting for reinsurance contracts held and transition requirements in the future. The OIC member agreed that the Board should consider the suggestions developed by the ANC.

61. Two ASAF members (ANC and ASBJ) welcomed the Board's tentative decision to propose a one-year deferral of the effective date of IFRS 17 and suggested that the Board should consider any implications on this decision when the amendments to IFRS 17 are finalised.

Management Commentary

62. The objective of this session was to provide an update to the ASAF members on the Board's tentative decision on the objective of management commentary as part of the update to IFRS Practice Statement 1 *Management Commentary* (Practice Statement), and receive their advice on the suggested proposals by the staff included in Agenda Paper 5 on:

   (a) applying materiality in preparing management commentary; and

   (b) principles for preparing management commentary.

Applying materiality in preparing Management Commentary

63. A third of the ASAF members (EFRAG, FRC, ARD and ANC) expressed concerns on the proposed two-step approach for identifying material information for inclusion into management commentary. Their view was that identifying material information is a holistic and integrated process. In addition, the ANC member said that the two-step approach to identifying material information can be too broad or vague. The ANC

member recommended, that to avoid this, the updated Practice Statement includes examples on material information. For instance, information provided in the company's press releases is likely to be material and thus, should be included in the management commentary.

64. While the ARD member said that they have no objection to the proposal to distinguish between matters and information on those matters in the suggested two-step approach to identifying material information, they were of the view that such a distinction may be difficult in practice. In addition, the member agreed that the materiality concept used for management commentary should be consistent with IFRS Practice Statement 2 *Making Materiality Judgements,* because the management commentary is an additional narrative of financial information and therefore, it should follow the same guidance as for financial statements.

65. The EFRAG member said that the materiality judgements for management commentary may be different than for the financial statements. IFRS Standards determine the potential population of the information in the financial statements to a much greater extent, and therefore the materiality judgements for the financial statements is more of a filtering exercise. Identifying material information for the management commentary is different because its scope is broader. The member questioned whether the Practice Statement should ask for disclosures of 'material risks' or 'principal risks' and suggested that further tools or guidance would be needed so that preparers produce management commentaries which are not of excessive volume.

66. The FRC member noted that, while they agreed with the filter on what is material to the long-term success of the entity, they had some concerns about the discussion of the long-term success in terms of future cash flows. This approach could be associated with discounted cash flow methodology and could result in omitting from management commentary issues which are not material today. In response, the IASB Chair emphasised that the assessment of what is material cannot only be quantitative but also qualitative.

67. The GLASS member noted that the reference to cash flows would most likely be interpreted as precise forecasts rather than a discussion on cash flows. They were also of the view that identifying material information by reference to cash flows may be

difficult or not appropriate for some industries (eg financial institutions) and a profitability analysis may be more important. They also noted that the reference to forecasts in the illustrations provided in the materials seemed to imply a request for earnings guidance, which is subject to different local regulations. The member suggested that it should be clear that earnings guidance is not required as part of management commentary. A Board member responded that some entities choose to express their strategy and future direction in a way that could be interpreted as earnings guidance, but there was a nuance in language which would need to be considered in the updated Practice Statement.

68. The AcSB member said that many companies in Canada have stopped providing guidance due to securities law but agreed with the Board members' comments on expressing strategy. Furthermore, the member advised that the management commentary should not only include quantitatively material information but also other information that has the potential to be material in later years.

69. The ANC member said that in France, there is a legal requirement that expects management commentary to provide information to a broader population of stakeholders than just to primary users. The member asked whether the materiality assessment for management commentary should take into consideration these other stakeholders.

70. The AOSSG member noted that AASB staff support the proposed distinction between matters and information about those matters.

Principles for preparing Management Commentary

71. The staff noted that all the qualitative characteristics identified in the *Conceptual Framework* are applicable to information in a management commentary, but that the materials provided highlighted those which the staff thought deserved particular emphasis or further clarity to be applied to the information in a management commentary.

72. Some ASAF members expressed their support for *coherence* or a *coherent narrative*, but did not consider it necessarily addresses or achieve completeness. The GLASS member agreed that a coherent narrative, which in their view included consistency, was important, but thought that a *complete* management commentary may be difficult to achieve. The ARD member stated that they had concerns that completeness could

deter from management's freedom to tell their story, as in their view, emphasising completeness seemed to imply following a template rather than including entity-specific information. The EFRAG member also noted they found it difficult to reconcile completeness with coherence, but instead associated the latter more with comparability. Both the ASBJ member and the FRC member expressed their agreement on the importance of coherence.

73. Most ASAF members (ANC, FRC, AOSSG, FASB, ARD, AcSB and EFRAG) expressed their views on the principle of *'comparability'* in management commentary:

    (a) The ANC member commented that comparability among competitors within a same industry can be difficult to achieve. The member added that while some industries do follow the same ratios and measures, this information may not be relevant for every company that has to disclose this information. In addition, the FRC member said that the challenge for achieving comparability is that companies provide metrics with the same name but are calculated differently. They also noted that it would be a challenge to specify how metrics are calculated since the Practice Statement is principles-based.

    (b) The AOSSG member suggested that management commentary should give freedom to the management to tell their own stories and these stories differed from company to company and industry to industry. Therefore, having a comparability principle can hinder inclusion of information from the eyes of management. Similarly, the FASB member added that management cannot have comparable views and perspectives.

    (c) The EFRAG member said that comparability can be hard to achieve, particularly in the narrative section. He also said that while comparability of metrics is desirable, it is unlikely the Board would want to define the metrics. The member questioned which company would be blamed if two companies' metrics are not comparable. In his view, because of such difficulties, caution is needed on using similar words applicable to financial statements which may not work well for management commentary.

(d) The AcSB member suggested that management commentary should focus on consistency and transparency of information because this puts users in the best position to assess comparability.

74. Most ASAF members (GLASS, AOSSG, ASBJ, FRC, FASB, AcSB, EFRAG and PAFA) commented on the principle of *'neutrality'* in management commentary, with a few members saying that the term 'balanced' may be more appropriate:

(a) The GLASS member said that an entity's management would be biased while providing information about their company and as a result, neutrality can be hard to achieve. The staff commented that the principle of neutrality is important so that negative information is not obscured but is given the same prominence as good news. The GLASS member responded that giving the full picture of the entity's performance is different from neutral presentation, which assumes independence of mind. He noted he would expect management commentary to include an appropriate view of risks of the business. In his view, a balanced view is not neutral, and balance may be a better word.

(b) Similarly, the FASB member said that the eyes of management are not neutral, and in their view, there is a natural tension between some of the qualitative characteristics.

(c) The ASBJ member shared a similar concern and asked that further explanation is provided on how neutrality ties into the concept of reporting through the eyes of management.

(d) The AOSSG member noted that Australian staff support the five aspects of neutrality noted in the paper, and that it is important for management commentary to be balanced so that it is not manipulated to be overly positive without disclosing the negatives.

(e) The FRC member said they agree with the sentiment of neutrality but are concerned with the word as it has a connotation of impartiality, which would imply not discussing the positives nor the negatives. The member noted that companies tend to be hesitant to report negative news because of market reactions, but in the member's view, what is important is for management to say what they are doing to rectify the issues where they are not performing so well.

(f) The AcSB member added that the word neutrality is understandable for standard setters, but it might not communicate the message that the Practice Statement is trying to convey to management. She said that the term 'balanced view' resonates more.

(g) The EFRAG member commented that completeness and neutrality are mutually supportive.

(h) The ANC member said that more importantly than neutral, management commentary should be factual and auditable.

(i) The PAFA member said that while wording may be an issue, in his view neutrality is not being 'middle of the road' but instead it is about being balanced and factual, and explaining both sides of the equation to enable users to make their own judgments.

75. Two Board members and the IASB Chair responded to the concerns raised. One Board member said that neutrality is about expecting management to look at results objectively to be able to make decisions – balanced without bias. The other Board member recognised that it can be hard to tell management to be neutral, and that preparers are not neutral by nature when talking about their own company, but the use and definition of the word for management commentary is the same as in the *Conceptual Framework*. The Board member said that emphasising neutrality is needed to address the prevalent issue shown from recent studies that the tone of management reports is biased and overly positive. The Board member also said that while balanced *view* is what neutrality aims to achieve, there is a risk of moving away from wording on neutrality and there could be implications for what that means for the use of neutrality in preparing financial statements. The IASB Chair said that similar challenges arise for the financial statements, but it is important that financial reporting is not skewed towards one outcome.

76. A few ASAF members shared their views on whether *'verifiability'* should be emphasised as a principle for management commentary as highlighted by the Management Commentary Consultative Group:

(a) The ASBJ member said that they support the idea of having forward-looking information in the management commentary, but would not recommend emphasising verifiability because forward-looking information is difficult to verify and, as a result, preparers would be deterred from providing such information.

(b) On the other hand, the ARD member supported the verifiability principle. The member said that information in the management commentary should be reliable because users use this information for decision making.

(c) The AOSSG member mentioned two comments raised by Australia and Korea. The member mentioned that both countries expressed different views on verifiability. Firstly, Australia agreed that the ability for information to be audited is important for the users. However, Korea disagrees with the proposal because it would be difficult to verify and provide assurance on forward-looking information and non-financial information. Additionally, including this principle could discourage management from disclosing the entity's story from their perspective.

Goodwill and Impairment

77. The objective of this session was to obtain ASAF members' advice on the disclosure objective and requirements. In addition ASAF members' views were sought on amortisation of goodwill, including whether members believe it is feasible to estimate the useful life of goodwill.

Improved disclosures for business combinations

78. ASAF members welcomed the enhanced disclosure requirements in relation to business combinations proposed by the staff during recent meetings of the Capital Markets Advisory Committee (CMAC) and the Global Preparers Forum (GPF). ASAF members had mixed views on the concerns of GPF members about the enhanced disclosure requirements. Specifically, the GLASS member did not share the concerns expressed by GPF members, emphasising that management should be held accountable for the decisions that they have made, and that it is surprising that management may not track or monitor such information.

79. Half of the ASAF members (KASB, FRC, ANC, ARD, EFRAG) expressed support for the staff's proposal for enhanced disclosures relating to business combinations and their subsequent performance. Comments by these members include:

(a) The KASB member suggested that the proposed disclosures could help users understand the financial effects of business combinations and provide users with some assurance about the recoverability of goodwill. The member also suggested enhancing IFRS 8 *Operating Segments* disclosure requirements to include the carrying amount of goodwill allocated to each segment, as well as disclosing separately the carrying amount of goodwill tested for impairment at segment level, and the carrying amount of goodwill tested at a lower level.

(b) The FRC member supported the disclosure objectives and stated that the enhanced disclosures would alleviate the pressure on the role of goodwill in providing stewardship information. The member also thought the concerns of GPF members were solvable as long as the requirements are not prescriptive and rely on the preparer to state the objectives of the business combination and how these are met over time.

(c) The ANC member agreed with the enhanced disclosures but thought that the proposals were missing management's final conclusion and justification of the carrying amount of the goodwill.

(d) The ARD member commented that enhanced disclosures would prompt management to exercise more caution when preparing forecasts, which would in turn lead to more timely recognition of goodwill impairments. However, the member further commented that auditors have expressed concerns that the proposed disclosures may contain sensitive information and may not be easily verifiable.

(e) The EFRAG member also agreed with taking an objective-based approach with flexibility to accommodate different acquisition strategies.

80. Some ASAF members, (ASBJ, OIC and some members of the AOSSG) shared concerns similar to those expressed by GPF members:

(a) The ASBJ member commented that companies update their KPI targets regularly and do not focus on the initial acquisition targets for their internal monitoring purposes and that they believe information on the subsequent performance of business combinations should be part of the management commentary.

(b) The OIC member thought the information would be sensitive and difficult to track.

(c) Some members of AOSSG expressed support for disclosures on subsequent performance but were concerned with the feasibility and cost of implementing the proposals. One AOSSG member suggested further outreach should be performed to understand the information entities could provide and some AOSSG members also thought the information should be part of the management commentary.

81. There were mixed views on whether the disclosures should be required only for some fundamental acquisitions. Specifically:

(a) The GLASS, FASB and AcSB members suggested assessing the materiality of the acquisition in the wider context of the corporate strategy. If the corporate strategy leads to a series of acquisitions, these acquisitions should be considered in aggregate.

(b) The EFRAG member commented that the focus should be not on the materiality of the acquisition, but rather on the materiality of the resulting disclosures.

(c) The OIC member commented that it is already difficult to make materiality judgements and cautioned against introducing another level of materiality.

(d) The FRC member commented that the disclosure required should be proportionate to the significance of the acquisition.

82. ASAF also discussed the further disclosure idea which would require entities to disclose its equity and profit or loss excluding the financial impacts of acquired intangible assets that would not be recognised if they had been generated internally and goodwill. ASAF member comments included:

(a) The ARD and the FRC disagreed with this idea because they were of the view that such information can be derived from information that is already available in the financial statements. The FRC member also commented that the disclosure may provide a solution for only some investors because different investors make different adjustments.

(b) The EFRAG member noted that the disclosure would require an entity to determine which acquired intangible assets would have qualified for recognition if they had been generated internally. That member suggested that there may be some practical difficulties in doing this because it would be difficult to avoid applying hindsight in assessing whether future economic benefits are probable.

(c) The AOSSG member commented that AOSSG members had mixed views on the usefulness of these further disclosure items.

Amortisation of goodwill

83. More members expressed support for amortisation of goodwill than those who did not. Some members supported amortisation from a conceptual stand point whereas other members stressed that they supported amortisation as a pragmatic solution rather than for its conceptual soundness. Specifically:

(a) The FRC member said goodwill is not an asset, but rather a residual that arises from a change in measurement bases. Nevertheless, he saw a case for amortisation of goodwill over the periods when the assets acquired are consumed because the measurement differences are also released over those periods.

(b) The ASBJ, OIC, ARD and some AOSSG members agreed with the view that the objective of the subsequent accounting for acquired goodwill is to reduce its carrying amount to zero as the benefits are consumed.

(c) The ASBJ member commented that amortisation would allow the allocation of the cost of the acquisition to the accounting periods in which the acquisition resulted in an increase in earnings. The member also indicated that not amortising goodwill leads, in effect, to the recognition of internally generated goodwill, which he thought should not be allowed because it contradicts the principles laid-out in IAS 38 *Intangible Assets*.

(d) The OIC and ARD members believe that amortisation would allow for better comparability between entities.

(e) Some AOSSG members thought that amortisation was a faithful representation of the asset's consumption. The ARD and some AOSSG members thought that amortisation was a pragmatic solution.

(f) The KASB member explained that benefits from goodwill will eventually reduce to zero but this is because it "disappears" at a point in time due to changes in external circumstances rather than being "consumed" over time. Subsequent measurement of goodwill is therefore a re-evaluation of existing goodwill in the cash-generating unit, rather than an allocation of historical cost to a period in a systematic fashion, like depreciation. The member believes, as a pragmatic solution, the Board could introduce a rebuttable presumption that the benefits from acquired goodwill will disappear over time. This would allow the carrying amount of goodwill to be reduced over time as if it was amortised.

(g) The FASB member stated that FASB Board members have mixed views on this topic. He explained the FASB will issue an invitation to comment that focuses on analysing the costs and benefits of amortisation, rather than conceptual arguments. The EFRAG member also agreed that further debates over the conceptual merits of amortisation are unlikely to be productive, and therefore has also viewed the issue from a cost benefit perspective.

(h) The AcSB member stressed that the Board should highlight that any decision to amortise goodwill would be based on a pragmatic consideration rather than conceptual arguments. This would help to reduce prolonged conceptual debates on the topic.

84. The ANC member commented that one of the arguments against amortisation was that it could distract attention from assessing whether the business combination was successful and an AOSSG member also did not support amortisation.

85. Regarding the determination of useful life of goodwill, ASAF members supported the following possibilities:

(a) A useful life prescribed by the Board (ARD, ASBJ).

(b) A useful life determined by management (ARD, ASBJ, AOSSG), perhaps subject to a cap prescribed by the Board (ARD).

(c) A useful life based on the weighted average useful life of the acquired assets (FRC, OIC) or the core assets of the cash generating unit (ARD).

(d) A useful life based on the payback period (OIC).

86. The FASB member had considered amortising over the weighted average life of the acquired assets but questioned whether this would work in all circumstances. The OIC member thought research should be performed regarding how the benefits are consumed.

87. ASAF members also made the following comments:

(a) The ARD member suggested the Board should expedite the project due to growing concern by regulators and the market over the large goodwill balances for listed entities in her jurisdiction. The member also observed that some companies had previously disagreed with amortisation but now support it.

(b) The EFRAG member stated that preparers supporting amortisation generally preferred the approach as a simpler alternative to the impairment only model. On the other hand, those preparers opposing amortisation are concerned that it will reduce entities' equity. The member also suggested that reintroducing amortisation could open up the possibility of replacing the mandatory annual impairment test of goodwill with a two-step approach.

(c) The GLASS member cited a study of reporting by financial institutions in Brazil. These financial institutions are required to present both goodwill under an impairment only model, as required under IFRS Standards, and an amortisation model, as required under Brazilian GAAP. The member commented that all analysts in the study added back the amount of amortisation recognised, suggesting that users generally think that amortisation does not provide useful information.

Update and agenda planning

88. The staff presented Agenda Paper 3, including the proposed agenda for the April 2019 ASAF meeting.

89. The ANC member proposed presenting how the ANC has established an accounting framework for crypto-currencies.

90. The EFRAG member suggested a future slot for EFRAG to present their forthcoming Discussion Paper on *Hybrid Pension Schemes*.

91. The staff will consider these suggestions for the future meetings.

Better Communication – Primary Financial Statements

92. The objective of this session was to:

    (a) provide ASAF members an overview of the Board's tentative decisions made to date in the Primary Financial Statements project; and

    (b) seek ASAF members' comments on the expected effects of the Board's tentative decisions.

Management Performance Measures (MPMs)

93. ASAF members were generally supportive of the Board's tentative decisions on MPMs. Most members said the Board's tentative decisions would improve economic decision-making by investors. However, AOSSG, KASB, ASBJ and ARD members said that providing tax and NCI effects for each adjustment would be costly for preparers.

94. The AOSSG member said some stakeholders, including credit analysts, thought the disclosure of tax and NCI effects would not be useful to users of financial statements. The staff and a Board member commented that different groups of users have different needs and buy-side analysts have been asking for such information.

95. The AcSB member said they heard strong support for most of the Board's tentative decisions on MPMs from their stakeholders including users and suggested that the Board's tentative decisions would bring MPMs to the attention of auditors and bring more rigour to such measures. However, the tentative decisions on tax and NCI disclosure was not supported by their stakeholders.

96. The AcSB member went on to say they were of the view that standard-setters should provide guidance on management-defined performance measures, as the quality of the information currently provided depends on the regulatory environment, which varies between jurisdictions.

97. The EFRAG member expressed support for the Board's tentative decisions but noted that regulators from different jurisdictions may hold different views on MPMs depending on their current practices. For example, regulators in countries where MPMs are only used outside financial statements may object to the tentative decisions.

98. The FRC member said MPMs fit better inside management commentary than in the financial statements. The FRC member said users are aware that information in the management commentary is often more subjective and subject to less assurance than information in the financial statements. However, the AcSB member suggested that users may not always be aware of these differences.

99. The ANC member said they were supportive of the Board's tentative decisions. The member said management-defined measures of performance would not be replaced by the required subtotals that could be proposed in this project. The member also asked the Board to clarify the relationship between the Board's tentative decisions on MPMs and IFRS 8 *Operating Segments*.

100. The FASB member encouraged the Board to provide more guidance on how the tax effects of MPM adjustments should be calculated. He suggested that the Board should either describe how to calculate the tax effects or explicitly state that entities can choose how to calculate the effects.

Subtotals

101. ASAF members were generally supportive of the Board's tentative decisions on subtotals. Most members said the tentative decisions on operating profit would improve economic decision-making by investors and would not be costly to implement.

102. However, KASB, ASBJ and AOSSG members said that some jurisdictions already define and require presentation of an operating profit, which differs from the Board's planned operating profit definition. The KASB member said they were concerned about the Board's planned definition, as they currently require entities to classify non-recurring income and expense items as non-operating. However, applying the Board's tentative decisions these items would be classified as operating. The ASBJ member said in Japan, operating profit excludes unusual items. A Board member and the staff clarified that the Board is aware of these different definitions of operating profit, but

in order to reduce diversity and bring more comparability, any definition proposed by the Board will result in a change for some.

103. ASBJ and ANC members suggested that the Board should describe the concepts that underpin each subtotal to be proposed. The staff clarified that the subtotals have underlying concepts but better communication of those concepts is needed.

104. FRC and ARD members said it is difficult to distinguish between integral and non-integral investments in associates and joint ventures. The ARD member expressed a preference for not making the distinction due to the level of judgement involved.

105. The FASB member asked in which category of the statement(s) of financial performance hedge accounting would be presented. A Board member clarified that the categorisation of income or expenses resulting from changes in the fair value of hedging instruments will depend on the categorisation of the income or expenses arising from the hedged asset or liability. Similarly, the categorisations of foreign exchange gains and losses will depend on the categorisation of the asset or liability that gives rise to the gains or losses.

106. The GLASS member said that some countries already have local laws that regulate the presentation of items in some categories of the statement(s) of financial performance.

107. The EFRAG member expressed support for the Board defining operating profit because operating profit is widely used in Europe but the definitions used are not consistent. He also supported defining operating profit as a residual because this approach is likely to be more feasible than a direct definition of operating profit. The member also asked how the draft proposals on the cash flow statement would apply to financial entities, and the staff said the Board will consider this in a future meeting.

Disaggregation

108. The ANC member said their stakeholders wanted to disaggregate expenses using a mix of functional and natural line items in some cases. The member also asked the Board to consider the possible implications of the draft proposals on disaggregation for the IFRS Taxonomy.