UPDATE
BOARD DECISIONS ON INTERNATIONAL ACCOUNTING STANDARDS

October 2001

Board Meeting Highlights

The International Accounting Standards Board met in Washington DC, USA, on 16-20 October 2001, where it:

- Met with the IASB Standards Advisory Council
- Discussed certain aspects of the Board's projects on:
  - Business Combinations
  - Improvements to Existing IASB Standards
  - Reporting Performance and
  - Share-based Payment.

Business Combinations

The Board considered whether the revised Standard should continue to permit, establishing as part of the apportionment of the cost of an acquisition, provisions for terminating or reducing the activities of the acquiree that were not liabilities of the acquiree at the date of acquisition. The Board tentatively agreed that provisions for terminating or reducing activities of the acquiree should be included as part of the apportionment of the cost of acquisition only when the acquiree has, as at the date of acquisition, an existing liability for restructuring costs recognised in accordance with IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. However, the Board agreed that it is open to further discussion of this issue when it considers issues related to the application of the purchase method together with the FASB as part of a joint IASB/FASB project.

The Board also reached tentative agreement on the following:

- IAS 27, *Consolidated Financial Statements and Accounting for Investments in Subsidiaries*, should be amended as part of the improvements project to require minority interests to be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity;
- The identifiable net assets acquired in a business combination should be measured by the acquirer at their fair values as at the date of acquisition, which is currently the allowed alternative treatment in IAS 22. This would mean that when an acquirer obtains less than a 100% ownership interest in an acquiree, any minority interest in the acquiree will be stated at the minority's proportion of the fair values of the acquiree's identifiable net assets. IAS 22's benchmark treatment, under which minority interest is measured at the minority's proportion of the pre-acquisition carrying amounts of the acquiree's identifiable net assets, would no longer be permitted;
- Acquisitions of some or all of the minority interests in a subsidiary by the parent, the subsidiary itself or another entity within the group should not be included in the scope of the revised standard. The accounting for such transactions will be considered further by the Board together with the FASB as part of a joint IASB/FASB project on issues related to the application of the purchase method;
- For any business combination, contingent liabilities of the acquiree (as defined in IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*) should be identified and recognised at fair value by the acquirer as part of the apportionment of the cost of acquisition, provided the fair values can be reliably measured;
- When the aggregate of the fair values of the identifiable net assets acquired in a business combination (including any contingent liabilities of the acquiree) exceeds the cost of acquisition, the acquirer should reassess the identification and measurement of those identifiable net assets. Any remaining excess should then be accounted for by:
  - First, reducing the carrying amounts recognised in respect of the acquiree's identifiable net assets that do not have a readily ascertainable market value. The Board will consider at a later meeting any guidance that should be included in the revised standard to clarify 'readily ascertainable market value'; and
  - Second, recognising the amount immediately in income as a gain;
- The level at which management identifies the group of cash generating units used for the purpose of the goodwill impairment test should be consistent with management's internal procedures for monitoring the return on the investment. However, that level should not be higher than a primary reportable segment level of the entity determined in accordance with IAS 14, *Segment Reporting*;

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- Goodwill acquired in a business combination should be tested for impairment before the end of the financial reporting period in which the business combination occurs by (a) calculating the recoverable amount of the cash generating unit(s) to which the goodwill is allocated and (b) comparing that recoverable amount with the carrying amount of the unit(s);
- Additional guidance on the use of present value techniques for determining the value in use of a cash generating unit(s) should be included as an appendix to the revised standard. That guidance will be based on guidance in FASB Concepts Statement 7, amended to reflect the measurement objective of value in use (rather than fair value as in Concepts Statement 7);
- A subsequent cash flow test should be performed for each of the five annual reporting periods following the impairment testing of goodwill based on projected future cash flows. This involves comparing actual cash flows achieved with those projected for the purposes of the goodwill impairment test and potentially requiring a write down if the actual cash flows would not have supported the carrying amount of goodwill. The Board will discuss the implications of this decision at a future meeting; and
- Reversals of impairment losses of goodwill should not be recognised.

The Board also reaffirmed its decision to consider as part of phase one of the business combinations project the date on which equity instruments issued as consideration should be measured. The Board agreed, however, that it would revisit this issue together with the FASB as part of a joint IASB/FASB project on issues related to the application of the purchase method.

Improvements to Existing IAS

The Board considered issues in respect of which international convergence and/or other improvements to the following International Accounting Standards could be made.

IAS 2, *Inventories*

The Board tentatively agreed to eliminate the last in first out method for determining inventory costs.

IAS 10, *Events After the Balance Sheet Date*

The Board tentatively agreed that when determining whether an enterprise should recognise a liability for dividends, IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, is applied.

IAS 16, *Property, Plant and Equipment*

- Income and related expenses of operations incidental to the construction or development of property, plant and equipment should be recognised in net profit or loss for the period
- The cost of acquisition of property, plant and equipment should include the estimated cost of dismantling and removing the asset and restoring the site, where that cost is recognised as a provision and represents either of the following:
  - the initial carrying amount of the provision
  - changes in the initial carrying amount of the provision that represent additional obligations unrelated to inventory or other production costs, or reflect changes in the estimated amount or timing of cash flows to settle the provision
- All exchanges of property, plant and equipment should be measured at fair value, i.e., as a disposal and an acquisition
- Subsequent expenditure relating to property, plant and equipment should be added to the carrying amount of the asset when the expenditure increases the asset's future economic benefits above those reflected in its most recent previously assessed standard of performance
- Depreciation of property, plant and equipment should cease when the property, plant and equipment is classified as held for sale.

IAS 24, *Related Party Disclosures*

- The definition of related parties should include parties with joint control over the reporting enterprise, and joint ventures in which the reporting enterprise is a joint venturer
- Parent-only financial statements issued separately should disclose related party transactions and outstanding balances that are eliminated in consolidated financial statements
- State-controlled enterprises should not be exempted from disclosing related party transactions with other state-controlled enterprises
- It should not be sufficient to disclose proportions of transactions and outstanding balances in respect of related parties – that is, disclosure of the amounts should be made
- The following additional disclosures should be made about outstanding balances with related parties:
  - the terms and conditions, including whether the amounts are secured, and the nature of any consideration to be provided in settlement
  - details of any guarantees given or received
  - provisions for doubtful debts
- Disclosure should be required for the bad or doubtful debts expense for the period in respect of debts due from related parties

- Disclosure of management compensation, expense allowances and similar items paid in the ordinary course of business should not be required
- Disclosure of pricing policies for related party transactions should not be required

The Board will consider draft exposure drafts incorporating these decisions at future meetings.

Reporting Performance

The Board had a preliminary discussion of certain matters related to reporting performance. The Board tentatively agreed that an entity should present a single statement of recognized income and expense as a component of a complete set of financial statements. The statement should include the effects of all changes in net assets during the period excluding those changes in net assets arising from transactions with owners in their capacity as owners.

The Board also tentatively agreed that there should be no 'recycling' of items of recognized income and expense.

The Board will continue its discussions of this project at a later meeting.

Share-Based Payment

The Board continued its discussions of accounting for share-based payment. The project is currently at a preliminary stage. Any tentative decisions made at this stage of the project are subject to reconsideration in the light of comments received from constituents as a result of the extended comment period on the Discussion Paper, *Accounting for Share-Based Payment*, released by the IASC and other G4+1 standard setters in July 2000.

The Board initiated discussions on measurement issues, focusing on the date of measurement (grant date, service date, vesting date or exercise date). The Board discussed the relationship between this issue, the reporting entity model (entity approach versus proprietary approach) and the distinction between liabilities and equity. No conclusions were reached. The Board agreed to continue its discussions at a later date.

In response to concerns raised by some commentators, the Board emphasised the need to address share-based payment. There is no existing standard either in international standards or in the large majority of national standards. There are concerns about the lack of standards in light of the increasing use of share-based payment, particularly in Europe. Various standard setters in Europe have been working on developing standards on the topic, and the IASB's constituents have emphasised the need to deal with this issue in a co-ordinated manner. Moreover, the International Organization of Securities Commissions (IOSCO) had identified this topic as one requiring attention, if international standards were to be globally accepted by securities regulators.

The Board noted that there were many complex issues to consider in developing a draft standard on share-based payment, and it would require time for careful consideration of all issues.