



IASB Update

From the International Accounting Standards Board

This IASB *Update* is a staff summary of the tentative decisions reached by the Board at a public meeting. As a project progresses, the Board can, and sometimes does, modify its earlier tentative decisions. Tentative decisions do not change existing requirements until those decisions are incorporated in a new or amended standard.

The International Accounting Standards Board met in London on 19 - 23 October 2009, when it discussed:

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Financial crisis

Consolidation

The Board continued its deliberations of the proposals in ED 10 *Consolidated Financial Statements* considering comments and information received from respondents to the exposure draft and from participants at the round table meetings held in June 2009.

The Board decided tentatively:

- to clarify that 'the activities' in the control definition are those activities of an entity that significantly affect the returns.
- to retain a broad definition and description of returns, similar to the description included in paragraphs 10 and 11 of ED10.
- to clarify the following regarding the returns element of the control definition:
 - a reporting entity must be exposed to variability of returns in the future
 - a reporting entity's returns can have the potential to be wholly positive, wholly negative or either positive or negative.
- to clarify the characteristics of power as follows:
 - power refers to a reporting entity's current ability to enforce its will in directing the activities of an entity that significantly affect the returns
 - power need not be exercised (this will be readdressed when the Board discusses power with less than half of the voting rights at a future Board meeting)
 - power need not be absolute

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Your feedback on IASB *Update*

Thank you to everyone who provided feedback on the new IASB *Update* format. Feedback was overwhelmingly positive but some adjustments need to be made, such as an improved print-friendly version. Our technology team is working hard on all the outstanding issues.

- o power is assessed on the basis of current facts and circumstances.
- that the final standard should include guidance discussing participating rights as follows:
 - o participating rights are rights that, if held by one party, are sufficient to give that party the ability to enforce its will in directing the activities of an entity that significantly affect the returns. If their exercise requires agreement by more than one party, participating rights prevent other parties from controlling the entity to which they relate.
 - o participating rights must be substantive.
 - o rights that are exercisable only when specified circumstances arise or events happen are participating rights in some circumstances and protective rights in others. The final standard will explain those circumstances.
- to retain the guidance on protective rights included in paragraphs B1 and B2 of ED10.
- that when two or more parties have discrete, unilateral decision-making authority over different activities of an entity, the party that has the ability to direct the activities that most significantly affect the returns meets the power element of the control definition.
- to clarify that understanding the purpose and design of an entity is an important factor to consider when assessing control of that entity, but that involvement in the design of an entity is not, in isolation, sufficient to conclude that the reporting entity controls that entity.
- that a reporting entity be required to assess control continuously and that the final standard should clarify the application of that requirement.

Agency relationships

The Board discussed when a party that has been delegated decision-making authority should be considered to be an agent. The Board did not reach any decisions on agency relationships.

This topic will be discussed further by the IASB and FASB at the joint meeting being held on 26-28 October. In November 2009, the Board will continue to deliberate the proposals in the exposure draft.

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Credit risk in liability measurement

The Board considered a summary of the responses to the discussion paper (DP) *Credit Risk in Liability Measurement*. The Board decided:

- to stop work on credit risk as a free-standing work stream.
- not to reach a general conclusion on credit risk at this time but instead to incorporate the topic in the conceptual framework measurement project;
- not to change the role of credit/performance risk in the definition of fair value as a result of the responses to the DP. The Board has not yet reviewed responses to the exposure draft *Fair Value Measurement*;
- to consider the application of the fair value definition in every project involving measurements that would otherwise be at fair value; and
- to consider the question of credit risk in every project involving a current measurement of liabilities that is not fair value.

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Derecognition

In March 2009 the Board published an exposure draft (ED) to replace the derecognition requirements in IAS 39 *Financial Instruments: Recognition and Measurement* and to improve the disclosure requirements in IFRS 7 *Financial Instruments: Disclosures* relating to the transfer of financial assets and liabilities. At this meeting the Board began redeliberation of the comments received on the ED.

The Board discussed:

- whether the derecognition model should include a test of bankruptcy remoteness ('legal isolation')
- whether sale and repurchase agreements ('repos') and similar transactions should be treated as sales or lending transactions

- how a transferor should treat (i) an interest that it retains in a previously recognised financial asset or (ii) an investment that it acquires in a transferee vehicle

The Board also discussed two possible approaches to replacing the current derecognition requirements for financial assets in IAS 39. One approach was a modified version of the current requirements in IAS 39, with the other being the alternative approach in the ED.

The Board tentively decided that a bankruptcy remoteness test should not form part of the derecognition model.

The Board was not convinced that all repos are sales. The Board therefore directed the staff to ascertain whether some repos (on the basis of the terms of those arrangements) are in substance lending arrangements.

The Board tentatively decided to pursue the alternative approach and directed the staff to further develop that approach to account for a retained interest as follows:

- a. If the retained interest is a disproportionate interest in the asset previously recognised, the transferor should treat it as a new asset and measure it initially at fair value but subsequently using the classification and measurement requirements in IAS 39. The transferor would recognise any gain or loss resulting from the transfer in profit or loss.
- b. If the retained interest is a proportionate interest in the asset previously recognised, the transferor should treat it as part of that asset. Therefore, the transferor would recognise a gain or loss only on the part transferred. The transferor would continue to measure the retained interest using the measurement basis that it applied to the asset recognised before the transfer.

The Board will continue the redeliberation of other aspects of the ED at future meetings

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Fair value measurement

The Board discussed the comment letters received on the exposure draft *Fair Value Measurement*. The comment deadline was 28 September 2009. The Board also discussed the preliminary project plan. The next steps are to hold round table meetings in the following locations:

- Norwalk: 2 November
- Tokyo: 27 November
- London: 11 December

In January 2010, the Board will start re-deliberating the issues raised in the comment letters and during the round-table discussions. The Board plans to issue an IFRS on fair value measurement in the third quarter of 2010.

The Board did not make any technical decisions at this meeting.

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Financial instruments

The Board continued to discuss responses received to its exposure draft *Financial Instruments: Classification and Measurement* (the ED), published in July 2009.

Classification and measurement - phase 1

Gains or losses related to Level 3 fair value measurements

The Board discussed whether entities should be required to present on the face of the statement of comprehensive income total gains or losses on financial instruments for the period for fair value measurements in Level 3 of the fair value hierarchy. Such amounts are already required to be disclosed IFRS 7, but not on the face of the statement of comprehensive income. The Board tentatively decided that the forthcoming IFRS on classification and measurement should not include a requirement to disclose this information on the face of the statement of comprehensive income. However, there was support to discuss this matter again at the joint meeting with the FASB in the

week beginning 26 October as part of the Financial Statement Presentation project.

Scope of the IFRS

The Board tentatively decided to exclude financial liabilities from the scope of the forthcoming IFRS. In the short term, the requirements of IAS 39 would continue to apply to financial liabilities. The Board asked the staff to further consider the accounting for financial liabilities and will address this issue in the near future.

Effective date and transition

The Board tentatively decided:

- that the effective date will be 1 January 2013 for the finalised guidance on classification and measurement of financial instruments.
- to permit early adoption of the final IFRS. In addition, the Board tentatively decided to require transition disclosures by all entities adopting the new IFRS, as proposed in the ED.
- to clarify the guidance in the ED on the 'date of initial application'.
- to permit, but not require, restatement of comparative periods by entities that implement the standard in 2009 or 2010. Comparative information will be required if an entity adopts the final guidance after 2010.
- to finalise the guidance on impracticability of retrospective application, as proposed in the ED. Accordingly, if it is impracticable for an entity to apply retrospectively the effective interest method or the impairment requirements for a financial instrument, the entity shall determine the amortised cost of the financial instrument, or any impairment on a financial asset, in each period, determined by using its fair value at the end of each comparative period.
- not to permit the continuation of separate accounting (bifurcation) for those hybrid contracts embedded in financial hosts that were bifurcated in accordance with the existing IAS 39.
- to remove the specific transition provisions on hedge accounting from the ED.
- that if an entity adopts the IFRS resulting from any phase of this project before its effective date, the entity (a) shall adopt all earlier phases before then, but (b) need not adopt later phases before their effective date.
- to finalise all other transition provisions as proposed in the ED.

Transitional insurance issues

The Board noted that insurers may face particular problems if they apply the new IFRS on classification and measurement of financial instruments before they apply the IFRS resulting from phase 2 of the project on insurance contracts. The Board tentatively decided:

- not to create a temporary exception permitting insurers to maintain the available-for-sale category temporarily until the phase 2 IFRS is available.
- to consider, in developing the transitional requirements for the phase 2 IFRS, whether to create a transitional option for an insurer to revisit the classification of financial assets when the insurer adopts the phase 2 IFRS. The Board noted that it had included such an option in IFRS 4 *Insurance Contracts* for reasons that are likely to be equally valid for phase 2.
- not to make any consequential amendments to IFRS 4 relating to shadow accounting for insurance contracts or for financial instruments containing a discretionary participation feature.

The Board expects to publish a final IFRS in November 2009.

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Financial statement presentation

At the October meeting, the board continued its deliberations on the proposals in the discussion paper *Preliminary Views on Financial Statement Presentation*. Specifically, the board considered:

- the classification of items of other comprehensive income on the statement of comprehensive income (agenda paper 5A);
- the allocation of income taxes on the statement of comprehensive income and the presentation of income taxes on the statement of financial position and the statement of cash flows (agenda paper 5B); and

- the disaggregation of items of income and expense by both function and nature on the statement of comprehensive income (agenda paper 5C).

Classification of items of other comprehensive income

The discussion paper proposes that items of other comprehensive income should be presented in a separate section that is displayed with prominence equal to that of all the other sections. It further states that for each item in other comprehensive income (except a foreign currency translation adjustment on a consolidated subsidiary and proportionately consolidated joint ventures), an entity should identify and indicate in the statement of comprehensive income whether the item relates to (or will relate to) an operating activity, investing activity, financing asset or financing liability. The Board tentatively decided to retain that proposal in the exposure draft.

Allocation and presentation of income taxes

The discussion paper proposes that an entity should apply existing requirements for allocating and presenting income taxes in the statement of comprehensive income. This may result in an entity presenting income tax expense or benefit in the discontinued operations and other comprehensive income sections of the statement of comprehensive income, in addition to determining the income tax effect for continuing operations. An entity should not allocate income taxes to either the business or financing sections, or to categories within those sections. The Board tentatively decided:

- to retain the proposal in the discussion paper that an entity should apply existing requirements for allocating and presenting income taxes in the statement of comprehensive income, including the requirement that an entity must present components of other comprehensive income either (i) net of related tax effects or (ii) before related tax effects.
- to retain the existing requirement that an entity must disclose the amount of income tax allocated to each component of other comprehensive income.
- to retain the proposal in the discussion paper that an entity must present current and deferred income tax assets and liabilities recognised in accordance with IFRSs or US GAAP, and related cash flows, in an income tax section on the statement of financial position and the statement of cash flows.

Disaggregation by function and nature

The discussion paper proposes that, within each category on the statement of comprehensive income, an entity must disaggregate its items of income and expense by function. *Function* refers to the primary activities in which an entity is engaged, such as selling goods, providing services, manufacturing, advertising, marketing, business development or administration. The discussion paper also proposes that each of those functions be further disaggregated by nature to the extent that information enhances the usefulness of the SCI in predicting an entity's future cash flows. If that by-nature presentation is impractical on the face of the SCI, an entity should present the information in the notes to financial statements. Nature refers to the economic characteristics or attributes that distinguish assets, liabilities, and income and expense items that respond differently to similar economic events. In an education session, the Board considered:

- whether to replace the discussion paper proposal with a disaggregation principle that requires an entity to consider disaggregation by-function, nature and measurement bases in the financial statements as a whole.
- whether an entity that has only one reportable segment should present its disaggregated information on the face of its primary statements.
- whether an entity that has more than one reportable segment should present its disaggregated information in its segment note.

The Board did not make a decision on the proposals for disaggregation at the October meeting. The presentation of disaggregated information will be reconsidered at the October joint meeting with the FASB.

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Insurance contracts

The Board discussed:

- unbundling
- deposit floor
- presenting income and expense

Unbundling

Some insurance contracts contain not just an insurance component, but also an investment (or financial) component or a service component (or both). The Board discussed whether an insurer should recognise and measure the components of a contract as if they were separate contracts (unbundling). The staff recommended an approach that depends on whether the components of a contract are interdependent. The Board directed the staff:

- to develop a more detailed explanation of the notion of interdependence.
- to clarify how this notion relates to the notion of contract segmentation being discussed in the project on revenue recognition.
- to consider whether this notion is similar to the notion that the fair value of a compound financial instrument may not equal the sum of the fair values of its components.

The Board will return to the topic of unbundling at a future meeting.

Deposit floor

In May 2009, the Board decided tentatively that the measurement of insurance contracts should include the expected (ie probability-weighted) cash flows resulting from those contracts, including the expected value of those cash flows whose amount or timing depends on whether policyholders exercise options in existing contracts (policyholder behaviour). The Board reconfirmed that decision. Applying that decision at this meeting, the Board confirmed that no deposit floor should apply in measuring insurance contracts. The staff will develop more specific proposals for identifying the boundary of an existing contract. Among other things, those proposals will consider:

- contracts known in some countries as 'universal life contracts'
- contracts that include an option for the policyholder to buy future insurance coverage.

Presenting income and expense

The Board also discussed how the performance statement (statement of comprehensive income) should present income and expense derived from insurance contracts. The main purpose of this discussion was to consider when (if ever) an insurer should recognise premium receipts as revenue and when (if ever) an insurer should recognise them as deposit receipts. The purpose of this discussion was educational and no decisions were made.

Next steps

The Board will continue its discussion of this project at the joint meeting with the FASB on 28 October.

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Liabilities: amendments to IAS 37

The Board discussed whether to re-expose for further comment its revised proposals for a new standard to replace IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. It decided tentatively to:

- publish a limited-scope document, exposing for comment its proposals to clarify the measurement requirements. The proposed clarifications are set out in Section 4.1 of Agenda Paper 7A;
- post on its website as early as possible in the comment period a working draft of the new standard, highlighting all other changes to the previous proposals; and
- in the published exposure document, alert constituents to the existence of the working draft standard and the nature of the other changes.

The Board aims to publish the limited-scope re-exposure document in December 2009 and to post the

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Other comprehensive income

The IASB and FASB projects on financial instruments are likely to add more items to other comprehensive income (OCI), making it increasingly difficult to compare an income statement prepared in accordance with the US GAAP with one prepared in accordance with IFRS. The main difficulty is the choice entities have in how and where they present components of OCI. Eliminating that choice will make it easier to compare income statements prepared in accordance with IFRS and will help identify points of difference between IFRS and US GAAP.

The Board therefore considered whether financial reporting would be improved by removing some of the options and choices available in IAS 1 *Presentation of Financial Statements* to entities applying IFRS.

The Board could foresee that if it supported the proposals to amend IAS 1 it would be preferable for the IASB and FASB to develop together exposure drafts to amend their respective requirements. This would allow the boards to expose the proposals at the same time and would provide potential respondents with the opportunity to see how such a proposal could help make it easier to compare IFRS and US GAAP compliant financial statements.

The staff emphasised, and the Board agreed, that nothing in the proposals would change which items can or must be presented in OCI or whether an item must be reclassified (ie recycled) upon derecognition. The main aspects of the proposals are simply to remove options.

The Board tentatively decided to eliminate the option in paragraph 81 of IAS 1 that permits an entity to present all items of income and expense recognised in a period in two statements: a statement displaying components of profit or loss (separate income statement) and a second statement beginning with profit or loss and displaying components of other comprehensive income (statement of comprehensive income). On this basis, entities would be required to present one statement of comprehensive income.

In making this tentative decision, the Board reaffirmed the current requirement in IAS 1 that the single statement of comprehensive income must be displayed with two sections: profit or loss and other comprehensive income. An entity would be able to change the title of these sections (as long as the meaning is clear) but the components of income displayed in each section may not be changed.

The Board also decided that:

- Components of OCI that will not be reclassified into profit or loss in future periods be displayed together and that components of OCI that might be reclassified into profit or loss in future periods be displayed together.
- The choice available to entities to report components of OCI either net or before income tax effects be retained. However, if an entity reports components of OCI before tax effects it must report the aggregate amount of income tax for each of the aggregate of components of OCI that will not be reclassified into profit or loss in future periods and components of OCI that might be reclassified into profit or loss.

Next steps

The Board will discuss this topic with the FASB at its joint meeting 26-28 October.

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Post-employment benefits

The Board discussed the following possible amendments to IFRIC 14 *IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* and IAS 19 *Employee Benefits*:

- prepayments of a minimum funding requirement

- discount rate for employee benefits
- termination benefits

Prepayments of a Minimum Funding Requirement

The Board discussed responses to its exposure draft (ED) *Prepayments of a Minimum Funding Requirement* (Amendments to IFRS 14), published in May 2009, and tentatively:

- confirmed the scope of the project as proposed in the ED
- confirmed the definitions proposed in the ED. However, the Board tentatively decided to propose clarifying that a minimum funding requirement must be enforceable in the forthcoming ED of proposed amendments to IAS 19.
- reinstated paragraph 22 of IFRIC 14.
- confirmed the transitional arrangements as proposed in the ED.
- decided to require entities to apply the amendments for annual periods beginning on or after 1 January 2011 with early adoption permitted.

Discount Rate for Employee Benefits

The Board discussed responses to the exposure draft *Discount Rate for Employee Benefits* (Amendments to IAS 19), published in August 2009. The responses to the ED indicated that the proposed amendment raised more complex issues than had been expected. The Board therefore decided to adhere to its original plan to address measurement issues only in the context of a fundamental review. Thus, the Board decided not to proceed with the amendment. This means that entities will still need to refer to a government bond rate when there is no deep market in high-quality corporate bonds.

Termination Benefits

In June 2005, the Board published an Exposure Draft of Amendments to IAS 19, dealing with the accounting for termination benefits, together with proposed amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. At this meeting, the Board tentatively:

- confirmed its previous decisions on termination benefits.
- decided that entities should apply the amendments for annual periods beginning on or after 1 January 2011 with early adoption permitted.
- decided it would publish the amendments to IAS 19 relating to termination benefits together with the amendments to IFRIC 14.

Next steps

The Board intends to publish final amendments to IFRIC 14 and IAS 19 in December 2009.

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Future Board meetings

The Board will meet in public session on the following dates in 2009. Meetings take place in London, UK, unless otherwise noted.

26-28 October (Joint meeting with FASB, Norwalk, US)

16-20 November

14-18 December

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ISSN 1474-2675