



## Welcome to IASB Update

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 17-21 May 2010. The US Financial Accounting Standards Board (FASB) joined the IASB for some sessions. The boards discussed:

- Annual improvements
- Conceptual framework: qualitative characteristics
- Consolidation
- Emissions trading schemes
- Financial instruments: hedge accounting
- IFRS Interpretations Committee update
- Insurance contracts
- Joint arrangements
- Leases
- Management commentary
- Revenue recognition

### Annual improvements

The IASB discussed proposals to revise the criteria for selecting amendments to IFRS for inclusion in the Annual Improvements project. Board members provided feedback to staff. The proposals will be presented to the Trustees in July.

[Go to the project page on the IASB website](#)

### Conceptual framework: qualitative characteristics

The IASB and FASB discussed two issues that arose from the ballot draft on the objective of financial reporting and the qualitative characteristics chapters. The boards decided that materiality is an entity-specific aspect of relevance rather than a constraint to be considered in setting financial reporting

#### Contact us

**International Accounting Standards Board**  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

Tel: +44 (0)20 7246 6410  
Fax: +44 (0)20 7246 6411  
E-mail: [iasb@iasb.org](mailto:iasb@iasb.org)  
Website: [www.iasb.org](http://www.iasb.org)

#### Future board meetings

The IASB meets at least once a month for up to five days.  
The next Board meetings in 2010 are:

**1 June**  
**10 June**  
**14 - 18 June**  
**19 - 23 July**  
**13 - 17 September**

To see all Board meetings for 2010, [click here](#).

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standards. The boards also discussed how best to describe the objective of financial reporting. The boards directed the staff to prepare a new ballot draft to reflect both the discussion of the objective and the results of the decision about materiality.

[Go to the project page on the IASB website](#)

## **Consolidation**

### **Investment companies**

The IASB and the FASB decided:

- a decision-maker should assess whether it controls regulated funds that it manages. It should make this assessment by using the agency guidance that applies to all decision-makers that have been delegated decision-making authority. Consequently, there is no need to include specific guidance for regulated funds.
- when preparing its consolidated financial statements, the parent of an investment company (if it is not an investment company itself) shall be prohibited from retaining the fair value accounting that is applied by an investment company subsidiary to that investment company's controlled investees.

Accordingly, a parent of an investment company is required to consolidate all entities that it controls, including those that are controlled by an investment company subsidiary, unless that parent is an investment company itself. The boards confirmed their previous tentative decision that an investment company should be required to measure investment in entities that it controls at fair value through profit or loss. Refer to IASB Update 19-23 April 2010 regarding the criteria to be considered an investment company. The boards will discuss separate presentation and transition at future meetings.

The IASB tentatively decided:

- to replace the list of entities referred to in paragraph 1 of IAS 28 *Investments in Associates* and paragraph 1 of IAS 31 *Interests in Joint Ventures* with the proposed criteria for an investment company that have been developed within the consolidation project. An investment company would be required to measure investments in associates and joint ventures at fair value through profit or loss.
- that it would not address the timing issue faced by investment companies that are first-time adopters of IFRS in 2011. The timing issue is set out in agenda paper 12B which was also discussed at this meeting.

The IASB asked the staff to conduct further research to identify whether the decision to replace the list of entities referred to in paragraph 1 of IAS 28 and paragraph 1 of IAS 31 would restrict the number of entities currently applying the scope exemption set out in those paragraphs. The Board also tentatively decided that:

- a parent of an investment company, on consolidating that investment company subsidiary, would be required to retain the fair value accounting applied by the investment company subsidiary to investments that it does not control, including investments in associates and joint ventures.

### **Transition (revised consolidation requirements)**

The IASB discussed the transition guidance for situations in which applying the revised consolidation requirements results in a reporting entity consolidating an entity that was previously not consolidated. The Board tentatively decided that a reporting entity should measure the assets, liabilities and non-controlling interests of a previously unconsolidated subsidiary as if that subsidiary had been

consolidated from the date when the reporting entity obtained control of the subsidiary, on the basis of the revised consolidation requirements. Alternatively, if this was impracticable, the reporting entity should apply the acquisition method in IFRS 3 *Business Combinations* at the beginning of the earliest period for which application of those requirements is practicable.

The Board also discussed the transition guidance for situations in which applying the revised consolidation requirements results in a reporting entity no longer consolidating an entity that was previously-consolidated. The Board tentatively decided that a reporting entity should measure the interest in a previously-consolidated entity as if the reporting entity had accounted for that interest from when it first became involved with, or no longer had control of, the entity. Alternatively, if this was impracticable, the reporting entity should derecognise the assets, liabilities and non-controlling interests of the previously-consolidated entity, and recognise any interest in the entity at fair value at the beginning of the earliest period for which application of those requirements is practicable.

The Board tentatively decided to permit early application of the revised consolidation requirements.

### **Separate presentation of consolidated assets and liabilities**

US GAAP currently requires a reporting entity to present those assets of a consolidated variable interest entity (VIE) that can only be used to settle obligations of the consolidated VIE on the statement of financial position separately from those liabilities of a consolidated VIE for which creditors (or beneficial interest holders) do not have recourse to the general credit of the reporting entity.

The Board tentatively decided not to require such separate presentation of consolidated assets and liabilities. The Board asked the staff to investigate whether it would be useful to require disclosure of restrictions on the reporting entity's ability to access the cash flows of consolidated assets that can be used only to settle particular liabilities. This will be discussed at the next joint board meeting.

[Go to the project page on the IASB website](#)

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## **Emissions trading schemes**

The IASB discussed the emissions trading scheme research paper written and presented by a former IASB Industry Fellow, Nikolaus Starbatty. The staff intend to publish the paper as a Staff Research Paper in the next few months, because they believe it will be a helpful resource for those interested in the joint project on emissions trading schemes. The Staff Research Paper will reflect the views of Nikolaus, who will be identified as the author. The Board did not make any technical decisions at this meeting, but instead provided Niko with comments on the paper. The research paper provides a description of the mechanisms and types of emissions trading schemes, as well as an outline of other types of regulation that restrict access to resources. The paper also provides a brief description of the joint project on emissions trading schemes. The Board requested that additional information be included in the research paper relating to the accounting issues in emissions trading schemes that the staff and the boards are currently debating.

[Go to the project page on the IASB website](#)

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## **Financial instruments: hedge accounting**

The IASB discussed the eligibility of groups of hedged items for designation in hedging relationships, including net positions and contractually-specified risk components. The discussion was in the context of the general hedge accounting model that the Board is developing.

### **Groups of hedged items including net positions**

As a first step in considering this issue, the Board tentatively decided that no group-specific eligibility criteria should apply to the examples presented. The examples included some groups of hedged items (including some net positions). The Board discussed the examples in the context of an earlier tentative decision to propose using the cash flow hedge accounting mechanism for fair value hedges. In that context, the Board tentatively decided to present amounts transferred as hedge accounting

adjustments between profit or loss and other comprehensive income in a separate income statement line for the net position hedge examples discussed. As the Board continues to discuss further examples of groups of hedged items, these tentative decisions will be reviewed.

### **Contractually specified risk components**

The Board tentatively decided that a contractually-specified risk component should be an eligible hedged item, irrespective of whether it is the component of a financial or a non-financial item.

[Go to the project page on the IASB website](#)

## **IFRS Interpretations Committee update**

The Board discussed the IFRS Interpretations Committee's meeting on 6 and 7 May 2010. Details of the meeting were published in IFRIC Update, available [here](#).

## **Insurance contracts**

### **Margins**

The boards further discussed the measurement approach for insurance contracts.

- By a narrow margin, the IASB tentatively selected an approach that includes a risk adjustment plus a residual margin;
- By a narrow margin, the FASB tentatively selected an approach that includes a single composite margin.

### **Risk adjustment**

The boards discussed the objective for a risk adjustment, together with draft supporting guidance, and tentatively decided:

- that the objective is to reflect the maximum amount that an insurer would rationally pay to be relieved of the risk, taking into consideration that the amount of benefits and claim costs actually paid may exceed the amount expected to be paid.
- that the guidance accompanying this objective should clarify that a risk adjustment would capture the level of uncertainty inherent in the cash flows from the insurance liability from the perspective of the insurer, rather than from the perspective of a market participant.
- to limit the range of available techniques to measure the risk adjustment. Staff will bring back at a future meeting a discussion on which techniques would be available for measuring the risk adjustment, including a further analysis on whether a cost of capital approach would meet the objective of the risk adjustment.

### **Composite margin**

The boards discussed how to amortise a composite margin and considered the application of two possible factors:

- the insurer's exposure from the provision of insurance coverage, and;
- the insurer's exposure from uncertainties related to future cash flows.

The boards tentatively decided that these factors should be implemented through the following formula:

(Premium allocated to current period + current period claims and benefits)

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(Total contract premium + total claims and benefits)

The boards also affirmed that an insurer should not adjust a composite margin for changes in cash flow estimates.

### **Level of Measurement**

The boards then discussed the issue of the level of measurement and tentatively decided:

- that an entity should measure any risk adjustment at a portfolio level of aggregation;
- to retain the definition of portfolio of contracts in the existing IFRS 4 as *Contracts that are subject to broadly similar risks and managed together as a single portfolio*; and
- that residual or composite margins should be determined at a cohort level of aggregation, by grouping insurance contracts by portfolio and, within the same portfolio, by date of inception of the contract and by length (or life) of the contract.

The boards asked the staff to investigate and recommend whether to require or permit the insurer to determine a composite margin on an individual contract basis rather than on a cohort basis.

### **Disclosures**

The boards tentatively approved disclosure requirements for the forthcoming exposure draft, including a principle on the level of disaggregation for disclosure purposes. The boards provided some comments for the staff to consider in drafting the proposed requirements.

### **Unbundling**

The boards discussed a possible guiding principle for unbundling, built around the notion of significant interdependence. They asked the staff to refine the guidance supporting the proposed principle so as to explain more clearly how an insurer would assess whether interdependence is significant. If the refined guidance cannot address this point, the boards may need to review the proposed principle at a future meeting. The boards tentatively decided that account balances of account-driven contracts should be unbundled. For this purpose, the characteristics of these contracts will be defined in accordance with the guidance in US GAAP in ASC Topic 944-20-15.

On embedded derivatives:

- the IASB decided tentatively that embedded derivatives should be unbundled when the IASB's existing standards on financial instruments would require this;
- the FASB decided tentatively that embedded derivatives should be unbundled using the unbundling principle being developed for insurance contracts.

In addition, the boards tentatively decided that unbundling should be prohibited except in cases where it was required.

### **Scope**

The boards tentatively decided that the scope of the future standard on Insurance Contracts should:

- exclude fixed-fee service contracts;
- not exclude financial guarantee contracts, defined as contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

The boards noted that the proposed definition of an insurance contract:

- captures financial guarantee contracts, as defined above, but
- does not capture contracts that pay out regardless of whether the counterparty holds the underlying debt instrument, and
- does not capture contracts that pay out on a change in credit rating or change in credit index, rather than on the failure of a specified debtor to make payments when due. Thus, financial guarantee contracts, as defined above, would be within the scope of the standard on insurance contracts. The contracts described in the second and third bullets above would be within the scope of standards on financial instruments.

Thus, financial guarantee contracts, as defined above, would be within the scope of the standard on insurance contracts. The contracts described in the second and third bullets above would be within the scope of standards on financial instruments.

### **Next steps**

The boards will continue their discussion of this project at the joint board meeting on 1 June.

[Go to the project page on the IASB website](#)

## **Joint arrangements**

### **Interaction between IFRS 5 and loss of joint control/significant influence**

The IASB tentatively decided that when an entity partially disposes of an interest in a joint venture or in an associate it shall reclassify as held for sale only the interest disposed of if such partial disposal fulfils the criteria for classification as held for sale set out in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. The retained interest should continue to be accounted for using the equity method until the disposal occurs.

The Board also tentatively decided to extend the requirement of accounting for an interest in a joint operation that is classified as held for sale in accordance with IFRS 5 if an entity is committed to a sale plan that fulfils the criteria for classification as held for sale set out in IFRS 5.

The Board additionally agreed to clarify that if an interest (or a portion of an interest) in a joint venture or in an associate or an interest in a joint operation no longer meet the criteria to be classified as held for sale, an entity shall amend the financial statements for the periods since classification as held for sale.

### **Disclosures**

The Board tentatively decided:

- to replace the qualifier 'significant' by the qualifier 'individually material' in the disclosure requirement of a list and description of interests in joint arrangements and associates;
- that the summarised financial information for individually-material joint ventures and associates shall be presented on a hundred per cent basis and that an entity should disclose its net interest amount in those joint ventures and associates that are not individually material;
- that the summarised financial information provided by associates should include current assets, non-current assets, current liabilities, non-current liabilities, revenues and profit or loss;
- that an entity shall disclose commitments and contingent liabilities in relation to its joint ventures separately. There will be no requirement for an entity to disclose commitments and contingent liabilities in relation to its joint operations separately, because these will be included in the reporting entity's own disclosures; and
- not to specifically address which disclosure requirements venture capital organisations, or mutual funds, unit trusts and similar entities including investment-linked insurance funds need to fulfil in the case where these entities have an interest in a joint venture or an investment in an associate.

## Transitional provisions

The Board tentatively decided that the transitional provisions for Jointly Controlled Entities (JCEs) from the equity method to the accounting for share of assets and liabilities will consist in the derecognition of the investment, and the recognition of the shares of assets and liabilities at their carrying values based on the entity's interests determined in accordance with the contractual arrangement. Any difference between the carrying amount of the investment and the carrying net amount of the individual assets and liabilities will be recognised in retained earnings.

The Board additionally tentatively decided that an entity shall provide a reconciliation between the investment derecognised and the breakdown of the shares of assets and liabilities recognised, together with any balance recognised in retained earnings.

The Board also discussed transitional provisions for first-time adopters. The Board tentatively decided that the main difference between the transitional provisions for first-time adopters and for those entities reporting under IFRS will be:

- a first-time adopter will need to convert its investment in a jointly controlled entity to an IFRS basis; and that
- in the case of transitioning from proportionate consolidation to the equity method, the resulting investment will have to be tested for impairment in accordance with IAS 36 *Impairment of Assets* regardless of whether there is any existing indication that the investment might be impaired.

[Go to the project page on the IASB website](#)

## Leases

### Lessor accounting for the performance obligation

The IASB and FASB tentatively decided that under a performance obligation approach to lessor accounting, the lessor has a single performance obligation to continue to permit the lessee to use the leased asset over the lease term. That performance obligation would be satisfied, and revenue would be recognised, continuously over the lease term.

### Derecognition approach to lessor accounting

The boards discussed an alternative approach to lessor accounting, namely the derecognition approach. The boards then discussed two possible models - a full derecognition approach and a partial derecognition approach. If the boards adopt a derecognition approach to lessor accounting, the boards tentatively decided that in that case they would adopt a partial derecognition approach. Under the partial derecognition approach, the boards discussed:

- Accounting for residual assets
- Accounting for options.

### Accounting for residual assets

The boards tentatively decided that the residual asset would be an allocation of the previous carrying amount of the underlying asset. The residual asset would not be remeasured unless for impairment.

### Accounting for options

The boards tentatively decided that initial measurement of the residual asset recognised by the lessor would be based on the assessed lease term, ie the longest possible lease term that is more likely than not to occur.

The boards tentatively decided that accounting for a reassessment of the expected lease term would be

treated as a new derecognition/re-recognition event. That is, the lessor would derecognise/reinstate a portion of its residual asset. The boards asked the staff to provide additional analysis on accounting for purchase options under lessee and lessor accounting.

### **Accounting for contingent rentals and residual value guarantees**

The boards tentatively decided that changes in amounts receivable under all types of contingent rentals and residual value guarantees would be recognised in profit or loss.

### **Accounting for subleases**

The boards tentatively decided that different measurement guidance would not be provided for assets and liabilities arising from a sublease. Additionally, intermediate lessors would present all assets and liabilities arising from a sublease gross in the statement of financial position.

### **Presentation**

The boards tentatively decided that a lessor would present:

- lease receivables separately from other receivables in the statement of financial position
- residual assets separately together with property, plant and equipment in the statement of financial position with disclosures by class of assets
- revenue and cost of sales based on the lessor's business model; that is some lessors would present gross and other lessors would present net, in the statement of comprehensive income.

### **Disclosures**

The boards tentatively agreed to a set of disclosure requirements for lessors under the derecognition approach including the following:

- additional disclosures about the residual asset
- additional disclosures about the service obligations.

The boards asked the staff to consider the disclosure requirements in the Derecognition project. The FASB expressed a preference for the performance obligation approach for lessors. The IASB expressed a preference for a hybrid model in which the lessor would apply the derecognition approach for some leases and the performance obligation approach for others. The IASB asked the staff to develop proposals for deciding when to apply which model.

The boards will continue discussing lease accounting at the joint meeting in June.

[Go to the project page on the IASB website](#)

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## **Management commentary**

The IASB discussed the comment letters received on the exposure draft *Management Commentary*. The comment deadline was 1 March 2010. The Board did not make any technical decisions at this meeting.

### **Next steps**

The staff will continue to consider if there are issues that need to be re-deliberated by the Board. If there are no issues to be re-deliberated by the Board, the staff will begin the processes for finalising the document.

[Go to the project page on the IASB website](#)

## Revenue recognition

The IASB and FASB considered:

- repurchase agreements; and
- sales of assets that are not an output of an entity's ordinary activities.

### **Repurchase agreements**

The boards tentatively decided that the forthcoming Exposure Draft will explain how an entity would determine whether a buyer obtains control of an asset subject to a repurchase agreement:

- If a buyer has the unconditional right to require the entity to repurchase the asset (a put option), the buyer obtains control of the asset, and the entity should account for the agreement similarly to the sale of a product with a right of return.
- If an entity has an unconditional obligation or unconditional right to repurchase the asset (a forward or a call option), the buyer does not obtain control of the asset. The entity should account for the repurchase agreement as:
  - (a) a lease in accordance with *FASB Accounting Standards Codification* Topic 840 *Leases* or IAS 17 *Leases* if the entity repurchases the asset for less than the original sales price of the asset (ie the buyer pays a net amount of consideration to the entity).
  - (b) a financing arrangement if the entity repurchases the asset for more than the original sales price of the asset (ie the entity pays a net amount of consideration to the buyer).
- If the sale and repurchase agreement is a financing arrangement, the entity would continue to recognise the asset and would recognise a financial liability for any consideration received from the buyer. The entity would recognise the difference between the amount of consideration received from the buyer and the amount of consideration paid to the buyer as interest and, if applicable, as holding costs (eg insurance).

The FASB tentatively decided to remove Subtopic 470-40 *Debt - Product Financing Arrangements* from the Accounting Standards Codification.

### **Sales of assets that are not an output of an entity's ordinary activities**

The boards tentatively decided that an entity should apply the recognition and measurement principles of the proposed revenue model to contracts for the sale of the following assets that are not an output of the entity's ordinary activities:

- intangible assets within the scope of Topic 350 *Intangibles - Goodwill and Other* or IAS 38 *Intangible Assets*; and
- property, plant and equipment within the scope of Topic 360 *Property, Plant, and Equipment* or IAS 16 *Property, Plant and Equipment* or IAS 40 *Investment Property*.

Consequently, the entity would:

- derecognise the asset when the buyer obtains control of the asset, and
- recognise at that date a gain or loss equal to the difference between the transaction price and the carrying amount of the asset. The transaction price would be limited to amounts that can be reasonably estimated at the date of transfer.

### **Next steps**

The boards plan to publish the exposure draft in June.

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