IFRIC Update

From the IFRS Interpretations Committee

IFRS

November 2010

Welcome to the IFRIC Update

IFRIC Update is published as a convenience to the IASB's constituents. All conclusions reported are tentative and may be changed or modified at future IFRS Interpretations Committee meetings.

Decisions become final only after the Committee has taken a formal vote on an Interpretation or Draft Interpretation, which is confirmed by the IASB.

The Interpretations Committee met in London on **4 and 5 November**, when it discussed:

- Current agenda:
  - Vesting and non-vesting conditions
  - Put options written over non-controlling interests
- IFRS Interpretations Committee agenda decisions
- IFRS Interpretations Committee tentative agenda decisions
- Issues considered for *Annual Improvements*
- IFRS Interpretations Committee work in progress

The Committee also heard a presentation from the Autorité Des Normes Comptables (ANC - Standard Setter in France), on the outcome of its work performed on IFRS 2 Share-based Payment on behalf of the IASB. The objective is for the ANC to issue a research paper to show how core principles in IFRS 2 could be clarified so as to reduce complexity when applying the standard. The presentation from the ANC provided the Committee with a summary of its research findings.

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Future IFRS Interpretations Committee meetings

The next meetings are:
6 and 7 January 2011
10 and 11 March 2011
5 and 6 May 2011
7 and 8 July 2011
8 and 9 September 2011
3 and 4 November 2011

Archive of IFRS Interpretations Committee Newsletter

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Current agenda:

The Interpretations Committee discussed the following issues which are on its current agenda.

IFRS 2 *Share-based payment* - Vesting and non-vesting conditions

At the September 2010 meeting, the Committee completed its discussions on the technical issues included in this project, and decided to ask the Board for its recommendations on how to proceed. The Board subsequently requested the Committee to prioritise the issues being addressed by this project and consider the best path forward on an issue by issue basis.

At the November meeting, in response to the Board's request, the Committee decided to propose clarification to the definitions of service conditions and performance conditions through the next *Annual Improvements* cycle. The Committee identified the following as higher priority issues to be addressed in this way:

- the correlation between an employee's responsibility and the performance target
- whether a share market index target may constitute a performance condition
- whether a performance target that refers to a longer period than the required service period may

constitute a performance condition

- whether termination of employment is a forfeiture or cancellation event.

The Committee concluded that the following issues, however, should be referred to the Board for consideration in a future agenda proposal for IFRS 2:

- classification of a non-compete provision
- accounting for the interaction of multiple vesting conditions.

IAS 32 *Financial Instruments: Presentation* - Put options written over non-controlling interests

The Committee received a significant number of comment letters on the September 2010 tentative agenda decision relating to the request for guidance on how an entity should account for changes in the carrying amount of a financial liability for a put option, written over shares held by a non-controlling interest shareholder ('NCI put'), in the consolidated financial statements of a parent entity.

These comment letters highlighted the significant diversity in practice that exists in accounting for NCI puts and expressed support for either the Committee, or the Board, providing additional guidance on a timely basis.

The Committee also noted that in October 2010 the Board acknowledged that it currently does not have the capacity to devote the time necessary to deliberate issues relating to the *Financial Instruments with Characteristics of Equity* (FICE) project.

Consequently, the Committee decided to add this issue to its agenda, with the objective of addressing on a timely basis the current significant diversity that exists in practice. The Committee requested that the staff work with the FICE project team and consider potential alternative models for the accounting for NCI puts. In connection with this, the Committee asked the staff to seek the Board's views before the next meeting as to whether it should pursue alternatives, including applying derivative accounting for NCI puts, which might require an amendment to other IFRSs in order to implement.

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IFRS Interpretations Committee agenda decisions

The following explanation is published for information only and does not change existing IFRS requirements*. Committee agenda decisions are not Interpretations. Interpretations are determined only after extensive deliberation and due process, including a formal vote. Interpretations become final only when approved by the IASB.*

IAS 1 *Presentation of Financial Statements* – Current/non-current classification of a callable term loan

The Committee received a request on the classification of a liability as current or non-current when the liability is not scheduled for repayment within twelve months after the reporting period, but may be callable by the lender at any time without cause.

The Committee notes that paragraph 69(d) of IAS 1 requires that a liability must be classified as a current liability if the entity does not have the unconditional right at the reporting date to defer settlement for at least twelve months after the reporting period.

The Committee noted that IAS 1 provides sufficient guidance on the presentation of liabilities as current or non-current and that it does not expect diversity in practice. Consequently, the Committee decided not to add the issue to its agenda.

IAS 19 *Employee Benefits* – Accounting for a statutory employee profit-sharing arrangement

The Committee received a request for clarification of the accounting for a statutory employee profit-sharing arrangement that requires an entity to share 10 per cent of profit, calculated in accordance with tax law (subject to specific exceptions), with employees.

The Committee noted that although such a statutory employee profit sharing arrangement calculates amounts to be payable to employees in accordance with tax law, it meets the definition of an employee benefit and is in the scope of IAS 19. Therefore, the employee profit-sharing arrangement described in the request should not be accounted for by analogy to IAS 12 *Income Taxes* or IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

The Committee observed that the objective of IAS 19 is to record compensation expenses only when the employee has provided the related service. Consequently, an entity should not recognise an asset or liability related to future expected reversals of differences between taxable profit and accounting profit in connection with such an employee profit-sharing arrangement.

The Committee noted that the statutory employee profit-sharing arrangement described in the request should be accounted for in accordance with IAS 19, and that IAS 19 provides sufficient guidance on amounts that should be recognised and measured, with the result that significantly divergent interpretations are not expected in practice. Consequently, the Committee decided not to add this issue to its agenda.

IAS 36 *Impairment of Assets* - Calculation of value in use

The Committee received a request for clarification on whether estimated future cash flows expected to arise from dividends, that are calculated using dividend discount models (DDMs), are an appropriate cash flow projection when determining the calculation of value in use of a cash generating unit (CGU) in accordance with paragraph 33 of IAS 36.

The Committee noted that paragraphs 30–57 and paragraphs 74–79 of IAS 36 provide guidance on the principles to be applied in calculating value in use of a CGU. The Committee observed that calculations using a DDM which values shares at the discounted value of future dividend payments, may be appropriate when calculating value in use of a single asset, for example when an entity applies IAS 36 in determining whether an investment is impaired in the separate financial statements of an entity. The Committee understands that some DDMs may focus on future cash flows that are expected to be available for distribution to shareholders, rather than future cash flows from dividends. Such a DDM could be used to calculate value in use of a CGU in consolidated financial statements, if it is consistent with the principles and requirements in IAS 36.

The Committee noted that the current principles in IAS 36 relating to the calculation of value in use of a CGU are sufficient and that any guidance that it could provide would be in the nature of application guidance. Consequently, the Committee decided not to add the issue to its agenda.

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IFRS Interpretations Committee tentative agenda decisions

The Committee reviewed the following matter and tentatively decided that it should not be added to the Committee's agenda. This tentative decision, including recommended reasons for not adding the item to the Committee's agenda, will be reconsidered at the Committee meeting in January 2011. Constituents who disagree with the proposed reasons, or who believe that the explanations may contribute to divergent practices, are encouraged to communicate those concerns by ***13 December 2010*** *by email to:* ***ifric@ifrs.org****. Communications will be placed on the public record unless the writer requests confidentiality, supported by good reason, such as commercial confidence.*

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* – Inclusion of own credit risk in the discount rate

The Committee received a request for interpretation of the phrase 'risks specific to liability' and whether this means that an entity's own credit risk (performance risk) should be excluded from any adjustments made to the discount rate used to measure liabilities.

The Committee observed that paragraph 47 of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* states that 'risks specific to the liability' should be taken into account in measuring the liability, but that the guidance is not clear about whether an entity's own credit risk should or should not be included in the discount rate as a 'risk specific to the liability'.

The Committee noted that this request for guidance would be best addressed as part of the Board's project to replace IAS 37 with a new liabilities standard, and that the Board is already considering the request for additional guidance to be incorporated into this new standard. Consequently the Committee [decided] not to add this issue to its agenda.

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Issues considered for *Annual Improvements*

The Committee assists the IASB in Annual Improvements *by reviewing proposed improvements to IFRSs and making recommendations to the Board. Specifically, the Committee involvement includes reviewing and deliberating issues for their inclusion in future exposure drafts of proposed* Improvements to IFRSs *and deliberating the comments received on the exposure drafts. When the Committee has reached consensus on an issue included in* Annual Improvements*, the recommendation (including finalisation of the proposed amendment or removal from* Annual Improvements*) will be presented to the Board for discussion, in a public meeting, before being finalised. Approved* Improvements to IFRSs *(including exposure drafts and final standards) are issued by the Board.*

Issues recommended for inclusion in the 2010–2012 cycle for *Annual Improvements*

At its meeting in November 2010, the Committee deliberated the following issues and recommended the Board to add them to *Annual Improvements*. The Committee's recommendation will be submitted to the Board for discussion at a future Board meeting. If these issues are confirmed by the Board they will be included in the exposure draft of proposed *Improvements to IFRSs* which is expected to be published in the second half of 2011. The issues discussed were:

IAS 12 *Income Taxes* — Recognising deferred tax assets for unrealised losses on available-for-sale debt securities

In March 2010, the Committee received a request for guidance on how an entity determines, in accordance with IAS 12, whether to recognise a deferred tax asset relating to unrealised losses on available-for-sale debt securities ('AFS debt securities') that create a deductible temporary difference. At its meeting in May 2010, the Committee published a tentative decision not to take the issue onto its agenda. Since then, the staff have received several comment letters on the tentative decision and met with some of the interested parties.

At its November meeting, after previously discussing the issue further at its July and September meetings, the Committee discussed issues included in the comment letters received, and arising from outreach activities conducted by the staff.

Consequently the Committee recommends that the Board should amend IAS 12, as part of *Annual Improvements*, to clarify that:

- an entity assesses the probability of realising deferred tax assets by considering temporary differences on a combined basis for each type of taxable profit of the appropriate character (for example, ordinary income and capital gain) in a manner that is consistent with the rules established by the taxation authorities;
- the reversal of temporary differences without creating or increasing taxable profit in a particular period does not qualify as a tax planning opportunity; and
- taxable profits to be used in the assessment of whether to recognise a deferred tax asset should be those exclusive of reversal of the temporary differences and carryforwards, which are the subject of the assessment being made.

IAS 36 *Impairment of Assets* – Disclosure of the recoverable amount

The Committee received a request to address an inconsistency in the disclosure requirements for material impairments in IAS 36, when a discounted cash flow model is used in the calculation of the recoverable amount. The request proposes that disclosures be required of the discount rate used when discounted cash flows are used to calculate recoverable amount, whether this is based on fair value less costs to sell or value in use.

The Committee recommends that the Board should include the proposed amendment within the next exposure draft of proposed *Improvements to IFRSs*.

Issues with recommendations not to be added to *Annual Improvements*

The Committee deliberated two additional issues for consideration within *Annual Improvements*. The Committee decided not to recommend the Board to add the following issues to *Annual Improvements*:

IFRS 3 *Business Combinations* – Settlement of pre-existing relationships

The Committee received a request asking for clarification on the accounting for a pre-existing relationship that is not a reacquired right, between the acquirer and the acquiree in a business combination.

The Committee noted that paragraphs B51 to B52 of IFRS 3 and the illustrative example in paragraphs IE54 to IE57 of the Illustrative Examples to IFRS 3 are clear that the 'at-market' component of a pre-existing relationship, that is not a reacquired right, is included in goodwill following the business combination.

The Committee concluded that it did not expect significant diversity to arise in practice. Therefore, the Committee decided to propose that the Board should not add this issue to *Annual Improvements*.

IAS 41 *Agriculture* – Revenue on sale of agricultural produce

The Committee received a request to clarify the Illustrative Example 1 of IAS 41. The request asserts that the Illustrative Example 1 of the standard is unclear in its presentation in the Statement of comprehensive income, and that this has resulted in divergence in practice. The divergence arises from confusion about the application of the requirements for both the separate presentation of revenue under IAS 18 and the disclosure of gain or loss arising from the change in fair value less cost to sell of biological assets under IAS 41.

The Committee noted that the example is not meant to depict all of the disclosures that might be required in a complete set of financial statements, and that such fact is already stated in the introduction to Example 1. The Committee recommends that no action is taken in respect of this request as this is a matter of providing additional application guidance. The Committee noted that this issue may be considered in the future, if the Board decides to undertake a review of all Illustrative Examples within IFRSs. Therefore, the Committee decided to propose that the Board should not add this issue to *Annual Improvements*.

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IFRS Interpretations Committee work in progress

IAS 1 *Presentation of Financial Statements* – Current/non-current classification of debt (roll-over agreements)

The Committee received a request for guidance on the meaning of 'unconditional right to defer settlement' in paragraph 69(d) of IAS 1. In its deliberation the Committee also considered a practical application of the issue involving the classification of a short-term obligation (commercial paper) when it is backed by a long-term loan facility.

The Committee considered situations where an agreement was reached before the reporting date to refinance an existing borrowing with a different lender after the reporting date. There were mixed views among the Committee members as to whether the existing borrowing should be classified as current or non-current.

The Committee requested that the staff perform outreach on the topic in order to understand the level of diversity in practice, and to bring the issue back for further consideration at its meeting in January 2011.

IFRS 2 *Share-based Payment* – Share-based payment awards settled net of tax withholdings

The Committee received a request to consider the classification of a share-based payment transaction in which the entity withholds a specified portion of the shares that would otherwise be issued to the counterparty upon exercise (or vesting) of the share-based payment award. The shares are withheld by the entity in return for settling the counterparty's tax withholding obligation associated with the share-based payment.

The request received by the Committee asked whether the portion of the share-based payment that is withheld should be classified as cash-settled or equity-settled. This issue was discussed for the first time at the September 2010 Committee meeting, after which a tentative agenda decision was published. At its November meeting, the Committee considered the comment letters received on the tentative agenda decision. The Committee discussed the issue further and asked the staff to prepare some illustrative examples for it to discuss at a future meeting, with a view to deciding how it might address this issue through *Annual Improvements*.

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Committee outstanding issues update

The Committee received a report of outstanding issues.

With the exception of one issue, all requests received and considered by the staff were discussed at this meeting. The remaining issue is expected to be discussed at the January 2011Committee meeting.

Future IFRS Interpretations Committee meetings: 2011

The Committee's meetings are expected to take place in London, UK as follows:

- **6 and 7 January 2011**
- **10 and 11 March 2011**
- **5 and 6 May 2011**
- **7 and 8 July 2011**
- **8 and 9 September 2011**
- **3 and 4 November 2011**

Meeting dates, tentative agendas and additional details about the next meeting will also be posted to the IASB website at www.ifrs.org before the meeting. Instructions for submitting requests for Interpretations are given on the IASB website at:
http://www.ifrs.org/How+we+develop+Interpretations/Propose+an+agenda+item.htm.

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