IFRIC Update

From the IFRS Interpretations Committee

IFRS

May 2011

Welcome to the IFRIC Update

IFRIC Update is published as a convenience for 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 Interpretations 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 **5 and 6 May 2011**, when it discussed:

- Current agenda:
  - Accounting for stripping costs in the production phase of a surface mine
  - Contingent pricing of property, plant and equipment and intangible assets
- IFRS Interpretations Committee tentative agenda decisions
- Issues considered for Annual Improvements
- IFRS Interpretations Committee work in progress

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Future IFRS Interpretations Committee meetings

The next meetings are:
7 and 8 July 2011
8 and 9 September 2011
3 and 4 November 2011

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Current agenda:

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

IAS 16 *Property, Plant and Equipment*—accounting for stripping costs in the production phase of a surface mine

The Interpretations Committee took this issue onto its agenda in November 2009, and in August 2010 published for public comment a Draft Interpretation *Stripping Costs in the Production Phase of a Surface Mine*. The 90-day comment period ended on 30 November 2010. At the January 2011 meeting, the Committee discussed the comments received on the Draft Interpretation. At the March 2011 meeting, the Committee further deliberated the recognition and measurement principles of the stripping cost asset.

At the May 2011 meeting, the staff presented a revised draft of the Interpretation, and the Committee discussed the revised recognition and measurement principles. The Committee also discussed the issues of impairment of the stripping cost asset, transition considerations and whether to include the illustrative example in the final Interpretation.

The Committee tentatively agreed with the revised recognition principle. The Committee also tentatively agreed not to prescribe any specific cost allocation approach for the measurement of the stripping cost asset. Rather, the Committee tentatively agreed that a measurement principle based on production metrics was appropriate. The Committee also tentatively decided the following:

- that no guidance should be given on testing the stripping cost asset for impairment. Instead the guidance in IAS 36 *Impairment of Assets* should be applied. The Committee also discussed the need to assess the economics of the mine and whether abnormal or unusually high levels of waste extraction might indicate that the stripping costs do not, in fact, represent an asset;
- that any existing stripping cost asset balances at the date of transition, that cannot be directly associated with an identifiable component of the ore body, should be recognised in retained earnings at the beginning of the earliest period presented; and
- that no illustrative example should be included in the final Interpretation.

The Committee asked the staff to bring a final draft of the Interpretation to the next meeting.

IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*—contingent pricing of PPE and intangible assets

The Interpretations Committee took this issue onto its agenda in January 2011.

At the March 2011 meeting, the staff presented the main characteristics of contingent prices with the aim of outlining the scope of the project. At that meeting, the Committee also noted that the core issue is the accounting for the remeasurement of any liability recognised for the contingent price and whether that remeasurement should be recognised in profit or loss, or included as an adjustment to the cost of the asset.

At the May 2011 meeting, the Committee reviewed advantages and drawbacks of developing guidance by analogy to IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* and IFRS 3 *Business Combinations*. They also discussed the consequences for this project of the Board's recent decisions on the leases and revenue recognition projects.

The Committee decided to defer further work on this project until the Board concludes its discussions on the accounting for the liability for variable payments as part of the leases project.

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IFRS Interpretations Committee tentative agenda decisions

*The Interpretations Committee reviewed the following matters and tentatively decided that they should not be added to the Committee's agenda. These tentative decisions, including recommended reasons for not adding the items to the Committee's agenda, will be reconsidered at the Committee meeting in July 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 June 2011** 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 16 *Property, Plant and Equipment*—cost of testing

The Interpretations Committee received a request to clarify the accounting for sales proceeds from testing an asset before it is ready for commercial production. The fact pattern in the submission is of an industrial group with several autonomous plants being ready for their intended use at different times. This group is subject to a regulation that requires the group to identify a 'commercial production date' for the whole industrial complex. The question asked of the Committee is whether the proceeds from those plants already in operation can be offset against the costs of testing those plants that are not yet ready for their intended use.

The Committee noted that paragraph 17(e) of IAS 16 applies to an item of property, plant and equipment, and in relation to the fact pattern included in the submission, is likely to apply separately to each individual plant. They also observed that the 'commercial production date' referred to in the submission for the whole complex was a different concept from the 'ready for intended use' assessment in paragraph 16(b) of IAS 16. The Committee believes that the guidance in IAS 16 is sufficient to identify the date at which an item of property, plant and equipment is 'ready for intended use' and therefore to distinguish proceeds that offset costs of testing the asset from revenue from commercial production.

As a result, the Committee does not expect diversity to arise in practice and therefore [decided] not to add this issue to its agenda.

IAS 19 *Employee Benefits*—defined contribution plans with vesting conditions

The Interpretations Committee received a request seeking clarification on the impact that vesting conditions have on the accounting for defined contribution plans. Are contributions to such plans recognised as an expense in the period they are paid for or are they recognised over the vesting period? In the examples given in the submission, the employee's failure to meet a vesting condition could result in the refund of contributions to, or reductions in future contributions by, the employer.

The Committee noted from the definition of a defined contribution plan in paragraph 7 of IAS 19 and the explanation in paragraph BC5 of IAS 19 that vesting conditions do not have an impact on the classification of a plan as a defined contribution plan, if the employer is not required to make additional contributions to cover shortfalls because of these vesting conditions. In addition, the Committee noted from the guidance in paragraph 43 of IAS 19 that accounting for defined contribution plans means accounting for the reporting entity's obligation to pay contributions to the separate entity that runs the plan, but not accounting for the obligation to the employees who benefit from the plan. The Committee noted that accounting for defined contribution plans under IAS 19 focuses on the employer's obligation to make a contribution. Consequently, contributions to defined contribution plans are recognised as an expense or recognised as a liability (accrued expense) when they fall due and refunds are recognised as an asset and income when the entity/employer becomes entitled to them, e.g. by the employee failing to meet the vesting condition.

The Committee noted that there is no significant diversity in practice, and nor does it expect significant diversity in practice to emerge in the future. Consequently, the Committee [decided] not to add this issue to its agenda.

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Issues considered for Annual Improvements

The Interpretations Committee assists the IASB in Annual Improvements by reviewing proposed improvements to IFRSs and making recommendations to the Board. Specifically, the Committee's 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.*

In February 2011, the Trustees of the IFRS Foundation approved the addition of new paragraphs to the Due Process Handbook for the International Accounting Standards Board *(IASB Due Process Handbook) relating to the annual improvements process. The amendments to the IASB Due Process Handbook are intended to provide enhanced criteria to assist the IASB and interested parties in determining whether a matter relating to the clarification or correction of IFRSs should be addressed using the annual improvements process.*

Issues recommended for inclusion in the 2010-2012 cycle for Annual Improvements

At its meeting in May 2011, the Committee deliberated the following three 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* that is expected to be published in September 2011. The three issues discussed were:

IFRS 8 *Operating Segments*—reconciliation of segment assets in IFRS 8

The Interpretations Committee received a request to clarify in paragraph 28(c) of IFRS 8 that a reconciliation of the total of the reportable segments' assets to the entity's assets should be disclosed only if a measure of total assets for each reportable segment is regularly provided to the chief operating decision maker. This clarification would make this paragraph consistent with paragraphs 23 and 28(d) of IFRS 8.

The Committee agreed with the proposed clarification and decided to recommend that the Board should propose an amendment, through Annual Improvements, to paragraph 28(c) of IFRS 8 to confirm the view that a reconciliation of the total of the reportable segments' assets to the entity's assets shall be disclosed only if a measure of total assets for each reportable segment is regularly provided to the chief operating decision maker.

IAS 7 *Statement of Cash Flows*—classification of interest paid that is capitalised as part of the cost of an asset

The Interpretations Committee received a request to clarify the classification in the cash flow statement of interest paid that is capitalised into the cost of property, plant and equipment. Paragraph 16 of IAS 7 was understood to require interest paid that is capitalised to be classified as an investing cash flow. The Committee was informed that this seemed inconsistent with paragraphs 32 and 33 of IAS 7, which required interest paid to be classified only as an operating or a financing cash flow.

The Committee noted that the classification of payments of interest that are capitalised in accordance with IAS 23 *Borrowing Costs* should be classified in a manner that is consistent with the classification of the underlying asset to which those payments were capitalised. For example, payments of interest that are capitalised as part of the cost of property, plant and equipment should be classified as part of an entity's investing activities; payments of interest that are capitalised as part of the cost of inventories should be classified as part of an entity's operating activities.

Consequently, to eliminate the noted conflict in the classification guidance for payments of interest that are capitalised, the Committee decided to recommend that the Board should amend, through the annual improvements process, IAS 7 to clarify that the classification of payments of interest that are capitalised shall be classified in a manner consistent with the classification of the underlying asset to which those payments were capitalised.

IAS 16 *Property, Plant and Equipment*—revaluation model and proportionate restatement

The Interpretations Committee received a request to address a concern arising from the use of the revaluation method. More specifically, the concern relates to the guidance in paragraph 35(a) of IAS 16 relating to the computation of the accumulated depreciation at the date of the revaluation.

The Committee noted that requiring that the accumulated depreciation and the gross carrying amount to be restated proportionately when applying paragraph 35(a) of IAS 16 does not accommodate the effects of past revisions to residual value, useful life or depreciation method. The Committee also noted that paragraph 80(a) of IAS 38 *Intangible Assets* contains the same requirements.

Consequently, the Committee decided to recommend that the Board should amend paragraph 35(a) of IAS 16 and paragraph 80(a) of IAS 38 through Annual Improvements to reflect the fact that restatement of the accumulated depreciation is not always proportionate to the change in the gross carrying amount of the asset.

Issues with recommendations not to be added to Annual Improvements

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

IFRS 2 *Share-based Payment*—modification of a share-based payment from cash-settled to equity-settled

The Interpretations Committee received a request to clarify how to measure and account for a share-based payment in situations where a cash-settled award is cancelled and is replaced by a new equity-settled award and the replacement award has a higher fair value than the original award.

The Committee observed that amendments that would be necessary to IFRS 2 to provide specific guidance on this matter would be beyond the scope of the Annual Improvements project and would be better suited to being addressed as part of a separate IASB project to improve IFRS 2.

Consequently, the Committee decided to propose that the Board should not add this issue to Annual Improvements and instead recommended that this issue should be considered by the IASB as part of a future agenda proposal for IFRS 2.

IAS 27 *Consolidated and Separate Financial Statements*—contributions to a jointly controlled entity or an associate

The Interpretations Committee received three requests asking for clarification of the accounting when a parent loses control over a subsidiary and that subsidiary is contributed so as to become (part of) a jointly controlled entity (JCE) or an associate. In particular, does the parent recognise the full gain or loss resulting from the transaction or only to the extent of the interests of the other equity holders in the JCE or the associate?

The Committee noted that there is an inconsistency between the guidance in IAS 27 and IAS 31 *Interests in Joint Ventures* together with SIC-13 *Jointly Controlled Entities – Non-Monetary Contributions by Venturers* for transactions where a parent contributes interests in a subsidiary to a JCE and this contribution results in a loss of control in the subsidiary by the parent. Paragraph 5 of SIC-13 restricts gains and losses arising from contributions of non monetary assets to a JCE to the extent of the interest attributable to the other equity holders in the JCE, whereas paragraph 34 of IAS 27 requires full profit or loss recognition on the loss of control.

The Committee noted that the Board had previously in December 2009 decided not to deal with the inconsistency within the joint venture project but to deal with it separately. The Committee also noted that there are broader issues in relation to contributions to a JCE or associate in general, particularly involving the loss of control when a subsidiary becomes a JCE or an associate. The Committee therefore concluded that this issue would be best resolved by referring it to the Board as part of a broader project on equity accounting. Consequently, the Committee decided to recommend that the Board should not add the issue to Annual Improvements.

IAS 28 *Investment in Associates*—equity method

The Interpretations Committee received a request to:

a. correct an unintended inconsistency between the requirements of paragraphs 2 and 11 of IAS 28 and IAS 1 *Presentation of Financial Statements* (revised 2007) regarding the description and application of the equity method. This inconsistency arose when IAS 1 made a consequential amendment to paragraph 11 of IAS 28 as part of the 2007 revision to IAS 1.

b. clarify the accounting for the investor's share of the other changes in the investee's net assets that are not the investor's share of the investee's profit or loss or other comprehensive income or that are not distributions received. For example, how to recognise the dilutive consequence for an investor of an associate of an increase in the percentage of ownership interest of another equity owner of the associate.

The Committee decided to recommend that the Board should not add this issue to Annual Improvements, and instead, to recommend that this issue should be considered by the Board as part of a broader project to address other issues that have been brought to the Committee's attention relating to IAS 28.

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IFRS Interpretations Committee work in progress

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets and IFRIC 6 Liabilities arising from Participating in a Specific Market-Waste Electrical and Electronic Equipment*—use of IFRIC 6 by analogy

The Interpretations Committee received a request to clarify whether, under certain circumstances, IFRIC 6 should be applied by analogy to other levies charged for participation in a market on a specified date to identify the event that gives rise to a liability. The concern raised relates to when a liability should be recognised.

The Committee observed that the levies presented in the submission are all different. Whether and how the consensus in IFRIC 6 would apply to them could vary depending upon the facts of each levy.

The Committee also noted that the issue raises the two following fundamental challenges:

- determining whether the obligating event is the participation in an activity on the date specified by the legislation, or whether other factors create an earlier obligation; and
- when the obligating event arises in the current annual period, determining the circumstances when an appropriate portion of the charge can be accrued at an interim reporting date.

The Committee directed the staff to review the guidance in IAS 37 on the timing of recognition of a liability and to perform further outreach activities to National Standard Setters to learn about what analysis has already been performed on similar levies that might be helpful to the Committee. The staff will present the results of this further work at the meeting in July 2011.

IFRIC 15 *Agreements for the Construction of Real Estate*—meaning of continuous transfer of control in real estate transactions

The Interpretations Committee received a request asking for clarification on the meaning of 'continuous transfer' referred to in IFRIC 15. The submission described the sale of residential apartments off plan and that, in some jurisdictions, relevant public authorities may be involved in addition to the direct parties to the sale and purchase transaction (ie the buyer and the developer). The role of such authorities is usually to protect the buyer if the developer defaults.

At the meeting in March 2011, the Committee asked for further input on this issue from interested parties.

At this meeting, the staff provided the Committee with an update of their outreach activities to the jurisdictions in which real estate sales agreements have the characteristics described in the original submission. The revenue recognition project team also provided the Committee with an update on the criteria from the Board's latest decisions that are intended to help determine when the transfer of control in a sales transaction takes place and more specifically whether a performance obligation is satisfied continuously.

The Committee was provided with an example of a situation that specifically illustrates the issue in the submission; they did not conclude for this example whether the conditions for continuous transfer would be met either under IFRIC 15 or under the Board's proposed new *Revenue* standard.

The Committee decided to defer further discussion on this matter until the criteria for the determination of the transfer of goods and services are finalised as part of the revenue recognition project.

Committee outstanding issues update

The Committee received a report on two outstanding issues.

With the exception of those issues, all requests received and considered by the staff were discussed at this meeting.

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