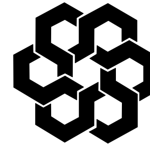

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International Accounting Standards Board

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.
These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting:	**November 2008, London**
Project:	**IFRS for Private Entities (formerly IFRS for SMEs)**
Subject:	**Redeliberation – Outstanding Issues in Other Sections (Agenda Paper 14B)**

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1. For the November 2008 Board meeting, the private entities agenda papers are organised as follows:
   - **Agenda Paper 14** – Overview
   - **Agenda Paper 14A** – Redeliberation of approach for income taxes (Section 28)
   - **Agenda Paper 14B** – Outstanding issues in other sections
2. Agenda Paper 14B sets out some of the issues from past Board papers that have been deferred, for example in areas where further research was being carried out, and also includes some new issues relating to areas where respondents requested further guidance, in particular in areas addressed by some IFRIC interpretations.
3. The issues in this paper are presented in numerical order. Those numbers are based on the section in the Exposure Draft (ED) of a proposed IFRS for SMEs to which the issue relates. Where issues have been deferred from past meetings, they have been given the same number as when they were first presented to the Board. All new issues are allocated a new number, ie one that has not been used for an issue in previous Board agenda papers.

4. The table on the following page provides a list of the issues presented in this paper for discussion. An issue is marked as 'new' if this is the first time the Board has seen it. All issues that have appeared in previous Board agenda papers are marked as "deferred".

Issue number	Title	New or revised issue
Section 19 Leases		
19.5	Agreements that contain a lease (IFRIC 4)	New
Section 22 Revenue		
22.2	Agreements for the construction of real estate (IFRIC 15)	New
Section 25 Share-based Payment (SBP)		
25.1	Equity-settled SBP – more simplification than just intrinsic value (including possibly disclosure only)	Deferred
25.2	SBP transactions with cash alternatives	New
25.3	SBPs where goods or services cannot be specifically identified (IFRIC 8)	New
25.4	Disclosure issues	New
Section 27 Employee Benefits		
27.1	Pensions – options for recognising actuarial gains and losses	Deferred
27.3	Pensions – measurement at current termination amount	Deferred
27.4	Pensions – allow choice of actuarial method	Deferred
27.5	Pensions – treat all multi-employer as defined contribution	Deferred
27.6	Pensions - Expected rate of return on assets	New
Section 35 Specialised Industries		
35.2	Service concession arrangements (IFRIC 12)	New
General issue		
G5	Title of the Standard	Deferred

Issue 19.5 (new): Leases – agreements that contain a lease (IFRIC 4)

5. **Comment letters.** Some comment letters recommended that the Board review the outstanding interpretations to identify those that address issues that should be covered in the IFRS for Private Entities. This is one such issue.

6. **Staff comment.** IFRIC 4 *Determining Whether an Arrangement Contains a Lease* specifies that some arrangements, such as outsourcing arrangements, telecommunication contracts that provide rights to capacity, and take-or-pay contracts, are in substance leases of assets, or contain leases of assets, and should be accounted for as such. The IASB's

SME ED is silent on these arrangements. Staff have been informed that in South Africa a number of small private entities have such arrangements. Before South Africa adopted the SME ED as its national standard for entities that meet the definition of 'limited interest companies', South African GAAP for such entities was IAS 17 *Leases* plus IFRIC 4. The silence on this matter in the ED has resulted in some South African private entities reversing their earlier accounting for these arrangements as leases. This matter has become a significant issue in implementing the ED in South Africa. It is likely to arise in other jurisdictions as well.

7. **Staff recommendation.** Staff believe that the principle in IFRIC 4 is appropriate for private entities. Therefore, staff propose adding the following paragraphs to Section 19 *Leases*:

19.X1 Some arrangements, such as outsourcing arrangements, telecommunication contracts that provide rights to capacity, and take-or-pay contracts, do not take the legal form of a lease but they convey rights to use assets in return for payments. Such arrangements are in substance leases of assets, and they should be accounted for under this section. An arrangement that meets both of the following criteria is, or contains, a lease that should be accounted for in accordance with this section:

(a) the arrangement can only be fulfilled by using a specific asset or assets (ie it is not economically feasible or practical for the supplier to fulfill its obligation through use of alternative assets).

(b) The arrangement conveys a right to control the use of the underlying asset. This is the case if any one of the following conditions is met:

(i) the purchaser in the arrangement has the ability or right to operate the asset or direct others to operate the asset (while obtaining or having access to more than an insignificant amount of the output of the asset).

(ii) the purchaser has the ability or right to control physical access to the asset (while obtaining or having access to more than an insignificant amount of the output of the asset).

(iii) there is only a remote possibility that parties other than the purchaser will take more than an insignificant amount of the output of the asset and the price that the purchaser will pay is neither fixed per unit of output nor equal to the current market price at the time of delivery.

19.X2 The assessment of whether an arrangement contains a lease is made at the earlier of the date of the arrangement and the date of commitment by the parties to the principal terms. A reassessment of the arrangement may be required in the event of a change in circumstances.

19.X3 For the purpose of applying the requirements of this section, the minimum lease payments include only payments for the lease (ie the right to use the asset) and exclude payments for other elements in the arrangement (eg for services and the cost of inputs).

Question 19.5

Does the Board agree with the staff recommendation to add the foregoing paragraphs 19.X1 to 19X3 to Section 19?

Section 22 Revenue

Issue 22.2 (new): Revenue – agreements for the construction of real estate (IFRIC 15)

8. **Comment letters.** Some comment letters recommended that the Board review the outstanding Interpretations to identify those that address issues that should be covered in the IFRS for Private Entities. This is one such issue.

9. **Staff comment.** IFRIC 15 *Agreements for the Construction of Real Estate*, provides guidance for the recognition of revenue by real estate developers for sales of units, such as apartments or houses, 'off plan' – that is, before construction is complete.

10. **Staff recommendation.** Staff believe that real estate developers often are private entities and that guidance on this matter should be included in the IFRS for Private Entities as an additional example in the Appendix to Section 22 *Revenue.* Staff propose adding the following example. Example 12 already addresses other aspects of real estate sales.

Example 12A Agreements for the Construction of Real Estate

22A.16A An entity that undertakes the construction of real estate, directly or through subcontractors, and that enters into an agreement with one or more buyers before construction is complete, shall account for the agreement as a sale of services, using the percentage of completion method, only if:

(a) the buyer is able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not); or

(b) the buyer acquires and supplies construction materials and the entity provides only construction services.

If the entity is required to provide services together with construction materials in order to perform its contractual obligation to deliver real estate to the buyer, the agreement shall be accounted for as the sale of goods. In this case, the agreement does not transfer to the buyer control and the significant risks and rewards of ownership of the work in progress in its current state as construction progresses. Rather, the transfer occurs only on delivery of the real estate to the buyer.

Question 22.2

Does the Board agree with the staff recommendation that an example on agreements for the construction of real estate should be added to the appendix in Section 22 as set out above?

Section 25 Share-based Payment

Background on Section 25

11. Section 25 of the ED addresses recognition of share-based payment (SBP) in paragraphs 25.2 and 25.3 (reproduced below) but then cross-refers to IFRS 2 *Share-based Payment* for the principles for measuring and disclosing equity-settled SBP, and also for measurement of SBP transactions with cash alternatives. In May 2008, the Board decided to eliminate cross-references to full IFRSs. Instead, the standard should address all requirements for SBP directly (and also directly address lessor accounting for finance leases, use of the fair value model for biological assets, and financial reporting in hyperinflationary economies).

12. Here are the two paragraphs in the ED relating to recognition of SBP transactions:

    Recognition

    25.2 An entity shall recognise the goods or services received or acquired in a share-based payment transaction when it obtains the goods or as the services are received. The entity shall recognise a corresponding increase in equity if the goods or services were received in an equity-settled share-based payment transaction, or a liability if the goods or services were acquired in a cash-settled share-based payment transaction.

    25.3 When the goods or services received or acquired in a share-based payment transaction do not qualify for recognition as assets, the entity shall recognise them as expenses.

13. The principles and guidance in IFRS 2 paragraphs 16-22 for measuring equity-settled SBP transactions by reference to the fair value of equity instruments granted are problematic for private entities because, in most cases, entity-specific observable market data, such as share prices and measures of volatility, are not available. The Board recognised this in IFRS 2 by providing a fallback – the intrinsic value method. However, most commentators on the ED and the Working Group (WG) on the IFRS for Private Entities felt that the intrinsic value method may be more of a complication, rather than a simplification, for private entities because it requires ongoing fair value measurements of private entities' equity instruments. Staff are, therefore, proposing to remove the fallback to intrinsic value (as measured at each reporting date) and instead replace it with a more appropriate simplification for private entities.

Issue 25.1: Equity-settled SBP – more simplification than just intrinsic value (including possibly disclosure only)

14. **Reason for revisiting issue.** This issue has not yet been discussed by the Board.

15. **Comment letters.** Simplify requirements – in many cases the intrinsic value method is not much of a simplification as this method requires knowing the fair value of the underlying equity share when the share option (or other SBP) is granted and at each subsequent reporting date. Possible simplifications include intrinsic value measured only at grant date (not updated) or substituting historical volatility of an appropriate industry sector index for expected volatility of a non-publicly accountable entity's share price in

an option-pricing model as per SFAS 123(R). Also, consider disclosure only for equity-settled share-based payments.

16. **Field tests.** Few field test entities had SBP transactions. Two had equity-settled SBP transactions, and they commented that they were unable to measure fair values of either the shares or the share options. A few entities that did not have any SBP transactions commented that they would have found Section 25 difficult had they needed to apply it.

17. **WG recommendation.** Most WG members felt that the intrinsic value method in IFRS 2 is not much of a simplification for private entities because it still involves determining the fair value of unquoted instruments and additionally requires this to be done every year. Many WG members who hold this view support a disclosure only approach. If the Board does not agree with the disclosure-only approach, WG members recommend that the Board seek further simplifications beyond the requirements of IFRS 2. WG members noted that a few comment letters provided ideas for simplification including:

    a. determining intrinsic value at grant date only,

    b. using the calculated value method like in the US standard SFAS 123(R), which also requires measurement only at grant date, and

    c. allowing subsidiaries to record a SBP expense on the basis of a reasonable allocation of the group charge when awards are granted by a parent company to the employees of different subsidiaries in the group.

    Some WG members felt that only determining intrinsic value at grant date would be an improvement on the current requirements. The other two methods above were not discussed.

18. **Further comments from the WG:** Paragraph 17 above sets out the WG's recommendation from their report which was based on discussions at the WG meeting on 10-11 April 2008. Since the WG report was presented to the Board at the May 2008 Board meeting (see Agenda Paper 9D from that meeting), staff have circulated to WG members a memo prepared by a corporate SBP expert which sets out some ideas for measuring equity-settled SBP transactions. Staff asked WG members for their views on the alternatives given in the memo. Of those WG members who replied, most were supportive of the following views:

    - It is very difficult to get a reliable fair value for unlisted entities. Many WG members reexpressed their support for a disclosure only requirement for equity-settled SBP schemes for this reason. One WG member noted that IAS 39.46(c) requires investments in equity instruments that do not have a quoted price and whose fair value cannot be reliably measured to be measured at cost and further noted that if it is hard for an investor to determine the fair value of such investments, it is equally difficult for the issuer to determine the fair value of options related to such securities.

    - It could be difficult for the IFRS for Private Entities to dictate only one valuation method for equity-settled SBPs since there are many ways of valuing share

prices/share options, eg using the price of recent investments, earnings multiples, net assets or discounted cash flows.

- One WG member suggested the following approach and circulated it to the WG. It was supported by most of the WG members who responded:

  > ED paragraph 25.4 should require that for equity-settled SBP transactions, an entity should measure the goods or services acquired and the increase in equity at the directors'/management's estimate of the fair value either directly of the goods or services acquired or indirectly through valuing the equity instruments granted. There should be a specific disclosure requirement for the entity to explain the methodology used to value the equity-settled SBPs. In other words, the directors/management would need to make a choice and disclose what they have done. The guidance notes or educational material accompanying the IFRS for Private Entities could discuss various methodologies. Such methodologies would include the option pricing models in IFRS 2, the intrinsic method, references to agreed prices for such investments including prices agreed with taxation authorities who require the use of fair values, etc. This approach would also allow subsidiaries to use the IFRS 2 methodologies.

19. **View of an external professional SBP valuation consultant on the staff recommendation** (in paragraphs 20 – 28). At the July 2008 meeting, staff reported to the Board that staff have asked a professional SBP valuation consultant for help in identifying issues and solutions relating to measurement of SBP by private entities. Excerpts from this person's comments are as follows:

    > My personal preference would be not to constrain a particular methodology, my fear being that where a particular approach is put forward it can become the default, without adequate consideration being given to the alternatives, even when another approach may, on balance, be preferable. Having said that, I can understand why you would want to do this and believe that the proposal leaves the door open to the use of other methods where that is appropriate.
    >
    > In terms of the fallback my view is that some accounting is better than no accounting (and disclosure only is quite close to no accounting) so I would favour the directors' estimate over no expense. I also believe that it is better to force management to take a view rather than to allow them to duck the issue; they are using these as remuneration therefore they must have some idea of what they are worth and it is helpful to the user of the accounts to be able to see how good or bad management's perception was. Having said that, I know that others would argue that where the results are so subjective then disclosure is the better alternative.

20. **Staff recommendation.** Staff propose that the first step should be to provide guidance on assessing whether SBPs are cash-settled or equity-settled. The outside experts on private entities' SBP plans with whom the staff consulted have pointed out that most SBPs made by private entities are actually cash-settled, rather than equity-settled. The experts noted that, because there is no public market for the shares of private entities, those shares that are actually issued to employees are normally repurchased by the entity,

often at an amount based on a formula derived from book values. In other cases, the entity has either a stated policy or past practice of settling in cash rather than issuing equity instruments at all. It is rare for private entities to make equity-settled SBPs since an employee would usually not be able to realise the value of the instruments.

21. Therefore, staff propose to include in the IFRS for Private Entities guidance that even if a SBP appears to be equity-settled, it may actually be cash-settled in substance as it will have been designed to enable the employee to realise the value of the instruments. For these and all other SBP transactions of private entities that are, in substance, cash settled, ED paragraphs 25.5 and 25.6 provide appropriate guidance for recognition and measurement, as follows:

    25.5 For cash-settled share-based payment transactions, an entity shall measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity shall remeasure the fair value of the liability at each reporting date and at the date of settlement, with any changes in fair value recognised in profit or loss for the period.

    25.6 For transactions with employees, if the equity instruments granted do not vest until the employees have completed a specified period of service, the entity shall recognise the services received as the employees render service during that period.

22. The outside experts have indicated that, normally, SBPs of private entities are truly equity-settled only where it is expected they will be ultimately realised by the employee due to an expected future IPO or sale of the business. For such cases, staff support the principle that an expense should be recognised and that the expense should be measured based on an estimate of the fair value of the SBP award at grant date whenever practicable.

23. Staff do not recommend a disclosure-only approach for equity-settled SBPs for the reasons given in BC 101 of the ED. Therefore staff suggest allowing disclosure only as a last resort where it is impracticable to determine both the fair value and the intrinsic value of the equity instruments at the grant date (see proposal in paragraph 26)

    BC101 Non-recognition is inconsistent with the definitions of the elements of financial statements, especially an expense. Moreover, users of financial statements generally hold the view that share-based payments to employees should be recognised as remuneration expense because (a) they are intended as remuneration, (b) they involve giving something of value in exchange for services, and (c) the consumption of the employee services received is an expense.

    In addition to raising measurement reliability and complexity concerns, commentators supporting a disclosure-only approach for equity-settled SBPs sometimes argued that there is no cost to the entity. In the staff's view, however, while there is no cash outlay, something of value has been given in exchange for services (as noted in BC101); hence, there is a cost. Moreover, arguing that share options are cost-free because no cash is involved would lead, illogically, to non-recognition of transactions involving other equity instruments (eg shares) and to equity instruments issued to parties other than employees (eg suppliers of goods or professional services). Private entities should estimate and recognise the compensation cost if at all practicable.

24. Where a private entity gives a true equity-settled SBP award, staff believe that the IFRS 2 approach for measuring equity-settled SBPs is overly complex for many private entities. Among other things, the benchmark is direct measurement of the fair value of equity instruments issued and, if that measurement cannot be made reliably, IFRS 2 requires use of intrinsic value (updated at each reporting date) or industry volatility measures. Indeed, many letters of comment on the ED said that the intrinsic value method can be more burdensome than determining the grant-date fair value of equity-settled SBPs, such as employee share options, because the intrinsic value (and hence the fair value of the shares) would need to be determined at each reporting date, not just at grant date. While some letters supported measuring intrinsic value of share options only at grant date, staff do not favour this approach unless it is impracticable to estimate the fair value of the share options reliably without undue cost or effort using either direct measurement or a 'calculated value'. This is because intrinsic value at grant date may simply be zero even though the share option is intended as compensation and the amount of compensation will often be substantial at exercise. Accordingly, in the outline in paragraph 26 below, staff have proposed requiring intrinsic value at grant date, supplemented by appropriate disclosure, if it is impracticable to determine the fair value of share options without undue cost or effort under an option-pricing model, e.g. it may be considered impracticable to estimate a suitable volatility measure without undue cost. Since an entity would only need to determine the intrinsic value once, it provides a simplification over the IFRS 2 intrinsic value method (hence staff see no need to also include the intrinsic value method, updated at each reporting date, as another type of 'fallback'). Under this approach the fair value of the shares at grant date would need to be determined and disclosed, and an expense would need to be recognised for any excess over exercise price. This would provide more useful information than simply disclosure only of the terms and conditions of the SBP transaction.

25. The compensation experts consulted by staff support requiring fair value measurement of all true equity settled SBP awards by private entities. One expert said that in many years of experience he has never encountered such an SBP award whose fair value could not be estimated reliably. This expert is a professional valuation consultant whose level of measurement expertise is likely to be substantially higher than that of financial officers of most private entities.

26. With the objectives of (a) keeping the basic principle of measuring equity-settled SBP based on the fair value of the SBP award at grant date whenever practicable and (b) simplifying the measurement for private entities, staff recommend that the following requirements for measurement of equity-settled SBP transactions are added to Section 25. (Note, this is only an outline of the staff's proposed approach. Staff will develop the wording for the final standard once the overall approach has been decided). The proposal is generally consistent with what is required by IFRS 2.17; however it would provide significantly more guidance than IFRS 2 does for unlisted entities and would also provide a default measurement method for those entities that do not have the experience in using or assessing different valuation methods. It is also consistent with the approach in FAS 123(R) for private entities:

25.X1 For equity-settled SBP transactions, the entity shall measure the goods or services received, and the corresponding increase in equity at the fair value of the goods or

services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity by reference to the fair value of the equity instruments granted. To apply this requirement to transactions with employees and others providing similar services, the entity shall measure the fair value of the services received by reference to the fair value of the equity instruments granted, because typically it is not possible to estimate reliably the fair value of the services received. The fair value of those equity instruments shall be measured at grant date.

Entity measures equity-settled SBP transactions by reference to the fair value of the equity instruments granted

Entity issues shares or share appreciation rights

25.X2 An entity shall measure shares or share appreciation rights using the following four-tier measurement hierarchy:

1. Directly measure the equity instruments granted using observable market prices (note that, in most cases, such prices will not be available for private entities).
2. Directly measure the equity instruments granted using entity specific observable market data such as (a) a recent transaction in the entity's shares or (b) a recent independent fair valuation of the entity or its principal assets.
3. Indirectly measure the share price using a valuation technique that uses market data to the greatest extent practicable to estimate what the price of those equity instruments would be on the grant date in an arm's length transaction between knowledgeable, willing parties.
   (a) There should be a rebuttable presumption that the Earnings Multiple method would provide the most reliable indirect measurement of the fair value of the entity's shares and hence it should be the default valuation technique. This presumption should be rebutted only in the circumstances described in (b) and (c) below. The Earnings Multiple method involves applying a market-based price-earnings multiple of a similar quoted entity to the entity's earnings to derive a value for the business (which can be used to estimate the fair value of the shares of the private entity). Guidance would be added on how to identify similar entities and on how to determine an appropriate earnings figure.
   (b) The presumption that the Earnings Multiple method would provide the most reliable measurement of the fair value of the entity's shares should be rebutted for the following types of entities:
      (i) Start-up entities or entities undergoing a period of significant change, since it will not normally be possible to determine an appropriate level of continuing earnings. A

discounted cash flow method should be used except in the circumstances described in (c) below.

(ii) Entities where the value of the business derives mainly from the underlying value of its assets rather than its earnings such as an investment holding business, eg a property holding company. A valuation technique using net assets should be used except in the circumstances described in (c) below.

(c) If in the judgement of the directors [management] of the entity a more reliable measure of the fair value of the entity's shares can be obtained by a different valuation technique than those prescribed in (a) or (b) above or if it is impracticable to use the techniques prescribed in (a) or (b), then directors should use their judgement to apply the most appropriate valuation method to determine the fair value of the entity's shares. Any valuation technique used should be consistent with generally accepted valuation methodologies for valuing equity instruments, and the entity should be required to disclose the reason for choosing the valuation methodology.

4. If it is impracticable to estimate the fair value of the share price reliably using any of the methods in paragraphs 25.X2(1) – (3) above, a disclosure only approach should be followed (disclosure would include the terms and conditions of the SBP, and an explanation why a reasonable estimate of fair value cannot be made).

<u>Share options</u>

25.X3 An entity shall measure share options using the following five-tier measurement hierarchy:

1. Directly measure the share options granted using observable market prices (note such prices will very rarely be available).

2. Directly measure the share options granted using entity specific observable market data such as a recent transaction in the entity's share options.

3. Indirectly measure the share option using an option pricing model. The inputs for the model should use market data to the greatest extent possible. The two inputs which are likely to be most problematic are the current price of the underlying shares and the expected volatility of the share price and these should be determined as follows:

(a) The share price should be determined following the steps in 25.X2(1)-(3).

(b) Historical volatility is the starting point (often surrogate) for expected volatility. If the share price is determined using the Earnings Multiple Method (the default valuation method under

25.X2(3)), the same data should be used to estimate volatility in the share price (ie the entity could use the historical or implied volatility of the similar listed entities). If the entity has not based its estimate of the share price on the share prices of similar listed entities, the entity should derive an estimate of expected volatility consistent with the alternative valuation methodology used. For example, if the entity values its shares on a net asset or earnings basis, it should consider the expected volatility of those net asset values or earnings.

4. If it is impracticable to estimate the fair value of the share options reliably without undue cost or effort using 25.X3(1) – (3) above, the share options should be measured at intrinsic value at grant date (i.e. measured only once) and supplementary disclosures should be provided (including disclosure of the share price even if an expense is not recognised).

5. If it is impracticable to estimate the fair value of the share price reliably using 25.X2(1) – (3) above in order to determine the intrinsic value under 25.X3(4), a disclosure only approach should be followed.

27. Staff acknowledge that one of the drawbacks of the Earnings Multiple method is that it focuses only on the entity's earnings. It ignores the entity's asset values and the ability of the entity to generate cash flows. However, staff feel the benefits of prescribing a default valuation technique, namely increased comparability and reduced opportunity to 'cherry pick' the valuation technique that achieves the best outcome for the entity outweigh this drawback. Staff opted for the Earnings Multiple method since the approach uses real fair market data that is readily available (this is consistent with the need to use market based inputs to the greatest extent possible when determining fair value) and it is based on the allowed approaches outlined in IFRS 2. Guidance will be added to explain that for the purposes of identifying similar entities, an entity would likely consider characteristics such as industry, business activities, markets served, stage of life cycle, size, location, financial leverage and applicable tax rate. Simple guidance will also be added on how to determine an appropriate earnings figure, for example adjustments should be made for finance costs and large non-reoccurring items in order to identify an appropriate level of maintainable earnings. Since real market data is used to establish the fair value, the same data can be used to estimate volatility for use in option valuation models when valuing share options (ie the entity could use the historical or implied volatility of the similar listed entities).

28. Regarding group arrangements, staff recommend allowing subsidiaries to record a SBP expense on the basis of a reasonable allocation of the group charge when awards are granted by a parent company to the employees of different subsidiaries in the group. Staff feel this would provide an appropriate simplification for private entities, since assumptions such as forfeiture rates and exercise behaviour may be more easily estimated for the employee population as a whole than for each individual subsidiary. Staff believe this simplification would not significantly reduce the usefulness of the information provided. This treatment should only be permitted when the parent prepares consolidated financial statements in accordance with IFRS for Private Entities or full IFRSs and appropriate disclosure of the basis of allocation is given.

Question 25.1A

Does the Board agree with the staff recommendation, in particular the outline of the staff's proposed approach in paragraph 26, which sets out a hierarchy for the measurement of equity-settled SBP transactions? In brief, if an entity measures equity-settled SBP transactions by reference to the fair value of the equity instruments granted and that fair value cannot be determined using observable market data, then the entity should use a valuation technique to estimate fair value (with the Earnings Multiple method as the default). Share options should be measured at intrinsic value at grant date, with supplementary disclosure, if the fair value of the share options cannot be determined without undue cost or effort. Only if it is impracticable to estimate the fair value of the share price (ie the intrinsic value cannot be measured reliably even at grant date) should a disclosure only approach be followed for equity-settled SBPs. There is no fallback to an intrinsic value approach where intrinsic value is updated at each reporting date, as in IFRS 2.

Question 25.1B

Does the Board agree with the staff recommendation that the ED should be amended to permit subsidiaries to record a share-based payment expense on the basis of a reasonable allocation of the group charge when awards are granted by a parent company to the employees of different subsidiaries in the group provided suitable disclosure is made and the parent entity presents consolidated financial statements under the IFRS for Private Entities or full IFRSs?

Issue 25.2 (new): SBP transactions with cash alternatives

29. **Additional staff issue.** Section 25 cross-refers to IFRS 2 *Share-based Payment* for the principles for measuring SBP transactions with cash alternatives. As noted in paragraph 11 above, in May 2008 the Board decided the standard should address all requirements for SBPs directly. Staff have presented their proposal on how to do this for SBP transactions with cash alternatives in paragraph 31 below.

30. **Staff comment.** ED paragraph 25.7 has the following requirements for SBP transactions with cash alternatives:

> 25.7 For share-based payment transactions in which the terms of the arrangement provide either the entity or the counterparty with the choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments, the entity shall account for that transaction, or the components of that transaction, as a cash-settled share-based payment transaction if, and to the extent that, the entity has incurred a liability to settle in cash or other assets, or as an equity-settled share-based payment transaction if, and to the extent that, no such liability has been incurred. An entity shall apply the procedures in IFRS 2 paragraphs 35–43 for measuring share-based payment transactions with cash alternatives.

31. **Staff recommendation.** As discussed in paragraph 20 above, most SBPs made by private entities are actually cash-settled, rather than equity-settled, to enable the counter-party to realise the value of the SBP. In particular where SBPs of private entities have cash alternatives, the cash alternative is usually taken. For this reason, and to respond to

concerns that the accounting for equity-settled SBPs is burdensome, staff propose simplifying the requirements for SBP transactions with cash alternatives by replacing ED paragraph 25.7 with the new paragraph below. In particular, these requirements provide relief from applying split accounting for SBP transactions where the counterparty has a choice of settlement.

25.7(new) Some share-based payment transactions give either the entity or the counterparty a choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments. In such a case, the entity shall account for the transaction as a cash-settled share-based payment transaction unless either (a) the entity has a past practice of settling by issuing equity instruments or (b) the option has no commercial substance because the cash settlement amount bears no relationship to, and is likely to be lower in value than, the fair value of the equity instrument. In circumstances (a) and (b), the transaction shall be accounted for as an equity-settled share-based payment transaction in accordance with paragraphs 25.X – 25.Y.

Question 25.2
Does the Board agree with the staff recommendation to replace the existing paragraph 25.7 in the ED with the new paragraph 25.7 above?

Issue 25.3 (new): SBPs where goods or services cannot be specifically identified (IFRIC 8)

32. **Comment letters.** Some comment letters recommended that the Board review the outstanding interpretations to identify those that address issues that should be covered in the IFRS for Private Entities. This is one such issue.

33. **Staff comment.** IFRIC 8 *Scope of IFRS 2* addresses whether IFRS 2 applies to transactions in which the entity cannot identify specifically some or all of the goods or services received. The SME ED is silent on these transactions. In South Africa, after IFRS 2 was adopted but before IFRIC 8 was adopted as national GAAP, Black Economic Empowerment share transactions were accepted to be outside IFRS 2, and these were generally not measured at fair value. When South Africa adopted IFRIC 8, these transactions were scoped into IFRS 2 and measured at fair value. Now, South Africa has adopted the SME ED as its national standard for entities that meet the definition of ‘limited interest companies’. The ED’s silence on this matter has resulted in some South African private entities resorting to the old (non-fair value) accounting. This matter has become a significant issue in implementing the ED in South Africa.

34. **Staff recommendation.** Staff believe that the principle in IFRIC 8 is appropriate for private entities. Staff also believe that the issue is likely to arise in jurisdictions other than South Africa. Therefore, staff propose adding the following paragraph to Section 25 *Share-based Payment*:

25.X Some jurisdictions have programmes established under law by which equity investors (such as employees) are able to acquire equity for apparently nil or inadequate consideration. This indicates that other consideration has been or will

be received (such as past or future employee services). These are equity-settled share-based payment transactions within the scope of this Section. Therefore, they must be measured at the fair value of the equity instruments granted unless it is impracticable to do so. The entity shall measure the unidentifiable goods or services received (or to be received) as the difference between the fair value of the share-based payment and the fair value of any identifiable goods or services received (or to be received) measured at the grant date.

Question 25.3

Does the Board agree with the staff recommendation to add the foregoing paragraph to Section 25?

Issue 25.4 (new): Disclosure issues

35. **Additional staff issue.** In September 2008 the Board redeliberated the disclosure issues in each section of the ED. However, discussion of the Section 25 disclosure issues was deferred pending discussion of the measurement of equity-settled SBPs.

36. **Staff comment.** Currently the ED contains minimal disclosure requirements for SBPs. If an entity has equity-settled SBPs, further disclosure requirements must be applied by cross-reference to IFRS 2. Since the Board has decided the standard should address all requirements for SBPs directly, the relevant IFRS 2 disclosure requirements need to be included within Section 25.

37. **Staff recommendation.** Staff propose that the Section 25 disclosures should be as follows (this is a complete list of the proposed disclosures for this section, and so it also includes the disclosures which are already in the ED):

25.X1 An entity shall disclose the following information about the nature and extent of share-based payment arrangements that existed during the period:

(a) a description of each type of share-based payment arrangement that existed at any time during the period, including the general terms and conditions of each arrangement, such as vesting requirements, the maximum term of options granted, and the method of settlement (eg whether in cash or equity). An entity with substantially similar types of share-based payment arrangements may aggregate this information.

(b) the number and weighted average exercise prices of share options for each of the following groups of options:

(i) outstanding at the beginning of the period;

(ii) granted during the period;

(iii) forfeited during the period;

(iv) exercised during the period;

(v) expired during the period;

(vi) outstanding at the end of the period; and

(vii) exercisable at the end of the period.

25.X2 For equity-settled share-based payment arrangements, an entity shall disclose information about how the fair value of goods or services received was measured.

25.X3 For cash-settled share-based payment arrangements, an entity shall disclose information about how the liability was measured.

25.X4 For share-based payment arrangements that were modified during the period, an entity shall disclose an explanation of those modifications;

25.X5 An entity shall disclose the following information about the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position:

(a) the total expense recognised for the period arising from share-based payment transactions in which the goods or services received did not qualify for recognition as assets and hence were recognised immediately as an expense, including separate disclosure of that portion of the total expense that arises from transactions accounted for as equity-settled share-based payment transactions;

(b) for liabilities arising from share-based payment transactions:

(i) the total carrying amount at the end of the period; and

(ii) the total intrinsic value at the end of the period of liabilities for which the counterparty's right to cash or other assets had vested by the end of the period (eg vested share appreciation rights).

Question 25.4

Does the Board agree with the staff recommendation for the Section 25 disclosures in 25.X1 to 25.X5 above?

Section 27 Employee Benefits

Issue 27.1: Pensions – options for recognising actuarial gains and losses

38. **Reason for revisiting issue.** At the May 2008 meeting, the Board decided that, in general, the accounting policy options in full IFRSs should be available to private entities. However, as an exception to this, at the July 2008 meeting the Board decided all actuarial gains and losses should be recognised immediately in profit or loss, as proposed in the ED. At the September 2008 meeting, some Board members suggested that the Board should revisit their decision on recognition of actuarial gains and losses at a future meeting.

39. **Comment letters.** Allow other options for actuarial gains and losses, in particular recognition outside profit or loss, such as in equity or in other comprehensive income. Give private entities all of the options that an entity has using full IFRSs.

40. **Field tests.** Only a few field test entities commented but those who did noted that expensing all actuarial gains and losses only had a small effect on profit or loss. Therefore, these entities were indifferent to whether or not alternative options were allowed for actuarial gains or losses and they considered the approach in Section 27 the easiest.

41. **WG recommendation.** WG members would allow all options for actuarial gains and losses that are permitted by IAS 19 *Employee Benefits*.

42. **Staff comment.** Currently Section 27 requires immediate recognition in profit or loss of all actuarial gains and losses. IAS 19 allows the following four options for recognising actuarial gains and losses (IAS 19.92–19.93A):

    a. Immediate recognition in profit or loss.

    b. Immediate recognition in other comprehensive income and presentation in a statement of other comprehensive income.

    c. The so-called 'corridor approach' in IAS 19.92, briefly summarised as recognition in profit or loss of the amortisation, over the average working life of the employees participating in a plan, of (a) the excess of (i) 10% of the defined benefit obligation and (ii) 10% of plan assets over (b) cumulative unrecognised actuarial gains and losses.

    d. Any other systematic method of amortisation that results in faster amortisation than the corridor approach.

43. **Staff recommendation.** Many of the comment letters that proposed allowing private entities more options for recognition of actuarial gains and losses, agreed that immediate recognition is the simpler option. However, their main concern was that immediate recognition in profit or loss would lead to volatility. Out of those respondents wanting more options for recognition of actuarial gains and losses, over half of them indicated that it is only important to include the IAS 19 option that allows immediate recognition in other comprehensive income. Paragraph BC 89 in the Basis for Conclusions notes that immediate recognition in other comprehensive income was not provided as an option in the ED since it "*requires preparation of a financial statement that most SMEs do not normally prepare*" (this would be the case if such entities presented other components of comprehensive income in the statement of changes in equity). In May 2008, the Board decided the final standard should incorporate the requirements of IAS 1 *Presentation of Financial Statements* (as revised in 2007). Under IAS 1 (revised) there is no option to present other components of comprehensive income in the statement of changes in equity. Instead, a statement of comprehensive income is required. Therefore, following requirements based on IAS 1(revised) would mean that immediate recognition of actuarial gains or losses in other comprehensive income would be feasible and not more burdensome for private entities than immediate recognition in profit or loss.

44. Of the four methods allowed in IAS 19 (see paragraph 42 above), immediate recognition in profit or loss or in other comprehensive income are the simplest methods for private entities to implement as they do not require tracking of data over many years and annual calculations. Immediate recognition also more faithfully presents the entity's pension obligation because it does not require deferral of actuarial gains and losses that do not

meet the definitions of assets or liabilities. In addition, financial statement users generally have told the Board that they find immediate recognition provides the most understandable and transparent information. Staff also note that in March 2008, the IASB published for comment a Discussion Paper *Preliminary Views on Amendments to IAS 19 Employee Benefits* and one of the Board's preliminary views in this paper is to recognise all changes in the value of plan assets and in the post-employment benefit obligation in the financial statements in the period in which they occur. This would mean removing the options for deferred recognition of actuarial gains and losses in defined benefit plans.

45. Staff do not propose introducing in the IFRS for Private Entities the options in IAS 19 that allow deferred recognition of actuarial gains and losses. Staff believe that not having the deferral options would improve the information available to users, whilst also simplifying requirements for preparers. Therefore a departure from full IFRSs can be justified both on a cost-benefits basis and a user-needs basis. However, the same argument cannot be used for prohibiting immediate recognition in other comprehensive income, provided that a statement of comprehensive income must be presented. Hence, staff propose that private entities should have the option to recognise actuarial gains and losses immediately in other comprehensive income.

<u>Question 27.1</u>

Does the Board agree with the staff recommendation that the ED should be amended to allow two methods for recognising actuarial gains and losses in the IFRS for Private Entities: immediate recognition in profit or loss and immediate recognition in other comprehensive income?

Issue 27.3: Pensions – measurement at current termination amount

46. **Reason for revisiting issue.** At the July 2008 Board meeting, the Board discussed whether, and in what circumstances, private entities might be allowed to measure the defined benefit obligation at a current termination amount, eg if information to apply the projected unit credit method as proposed in the ED was not available without undue cost. No decisions were made. The Board asked the staff to present a proposal at a future meeting that specifically sets out when a current termination amount might be used (ie when the undue cost and effort exemption could be used) and exactly how the current termination amount would be calculated, because current practice varies.

47. **Comment letters.** Measure as if all employees would retire as of the reporting date (that is, at a current termination amount) based on current salaries.

48. **Field tests.** Several field test entities have defined benefit plans. Some of these entities use outside specialists to value the plans so they did not encounter any problems. A few entities noted that use of outside specialists would be needed, but would be too costly. Another problem raised was the entities were unable to gather enough data to make estimates about demographic and financial variables as required by ED paragraph 27.16 for defined benefit plans.

49. **WG recommendation.** Most WG members would encourage the Board to simplify the calculation of defined benefit obligations. Some WG members suggested that the calculation could be simplified by measuring the obligation on the basis that all employees would retire at the reporting date.

50. **Staff recommendation.** Staff recommend that an 'undue cost or effort' exemption should be added to the requirement to apply defined benefit accounting when determining the defined benefit obligation of a defined benefit plan for private entities (similar to that used for fair value measurement of biological assets in ED paragraph 35.1). Staff propose that Section 27 should state that in either of the following cases the entity should measure the defined benefit obligation of a defined benefit plan at the current termination amount using current salary information:

    - when sufficient information is not available without undue cost or effort for an entity to determine the present value of its defined benefit obligation and related current service cost using the projected unit credit method; or
    - if using the projected unit method to determine the defined benefit obligation would not give meaningful information. For example, this may be the case if the plan has only a very small number of employees.

    This method would maintain the principles of recognising pension cost during the employees' periods of service and recognising an obligation for vested benefits, while simplifying the calculation. Since this exemption applies to the determination of the defined benefit obligation only, the entity would determine the fair value of plan assets in the usual way.

51. The current termination amount would be the vested benefit obligation at the balance sheet date assuming all employees were to terminate their employment as of that date, ie the present value of the payment stream that the pension scheme would have to pay current participants and their survivors if all employees were to leave on the reporting date. Hence, the current termination amount assumes that the plan continues and benefits are settled as they fall due. The requirements should make clear that the current termination amount is not the cost of settling the defined benefit obligation on the reporting date under an assumption that the plan is wound up.

52. The change in the current termination amount during the year would be recorded as the current year's pension expense. Calculating the current termination amount does not involve most of the complexity of needing to make actuarial assumptions of future variables that will affect the value of the pension obligation, eg future salary and benefit levels, and rates of employee turnover. However, the calculation would still require the use of mortality tables, appropriate discount rates, and an estimate of inflation for any index-linked benefits. It also would include the impact of legislation enacted prior to the reporting date. Furthermore, as the calculation simplification only applies to the defined benefit obligation, determination of the expected rate of return on assets would still be required (see Issue 27.6 below).

53. Guidance should be provided to ensure the 'undue cost or effort' exemption is applied appropriately. Section 27 should provide an explanation that the 'undue cost or effort' exemption can only be used in relation to the cost of obtaining information, e.g. costs of

hiring specialists, if the cost is significant in relation to the entity's other operating costs (note, an outside specialist would not be needed every year and significance should be judged in this context – see Issue 27.4 which proposes that a roll forward of the valuation may often be appropriate if actuarial assumptions are relatively constant).

54. Staff propose the 'undue cost or effort' exemption would apply on a plan by plan basis. However, an entity would not be allowed to apply the exemption in some years and not others (ie frequent changing between the two methods would not be allowed). If, in the past, the entity has used the 'undue cost or effort' exemption for a particular plan, and then has later moved back to applying defined benefit accounting for the defined benefit obligation of that plan, the entity would not be then be allowed to use the 'undue cost or effort' exemption again for that particular plan.

55. Recognition and measurement of defined benefit pension obligations provides useful information for users of financial statements. Staff do not favour or propose a disclosure only requirement for defined benefit plans due to concerns about off balance sheet obligations. However, staff feel that defined benefit accounting can be complex and costly for private entities and may not be applied correctly unless costly specialists are used. Staff also note that if the private entity only has very few employees, an assessment using the projected unit credit method would often not be appropriate. Staff believe that the current termination amount is an appropriate measurement simplification that provides users with useful information. If the exemption is taken, adequate disclosure about the defined benefit plan should be provided to explain the basis for determining the current termination amount.

<u>Question 27.3</u>

Does the Board agree with the staff recommendation to amend the ED to state that if sufficient information is not available without undue cost or effort to determine the present value of the defined benefit obligation and related current service cost under a defined benefit plan using the projected unit credit method, or determining the obligation that way would be of questionable usefulness because of the small number of employees involved, an entity should measure the defined benefit obligation of that plan at the current termination amount, defined as the vested benefit obligation at the balance sheet date assuming all employees were to terminate their employment as of that date using current salary information, and give supplementary disclosures?

Issue 27.4: Pensions – allow choice of actuarial method

56. **Reason for revisiting issue.** This issue has not yet been discussed by the Board as the outcome of the discussion on Issue 27.3 may affect Issue 27.4.

57. **Comment letters.** Do not require a specific actuarial method (projected unit credit). Also clarify that even if a specific method is required, an actuarial valuation performed by an outside actuary is not required to be done every year. Clarify that updating prior period valuations for changes in circumstances can result in reasonable measurements.

58. **Field tests.** See Issue 27.3.

59. **WG recommendation.** Most WG members would encourage the Board to seek simplify the calculation of defined benefit obligations.

60. **Staff recommendation.** If the Board agrees with the staff recommendation in Issue 27.3 to allow use of the current termination amount either if sufficient information is not available without undue cost or effort to apply defined benefit accounting for the defined benefit obligation or determining the defined benefit obligation that way would be of questionable usefulness because of the small number of employees involved, then staff do not feel there is any need to provide further simplification by allowing actuarial methods other than the projected unit credit method to be used.

61. Staff recommend clarifying the following where defined benefit accounting is applied to determine the defined benefit obligation (ie in the case where the undue cost or effort exemption is not appropriate in the staff recommendation for Issue 27.3):

    a. An actuarial valuation performed by an outside actuary is not required every year since often a roll forward of the valuation would be appropriate if actuarial assumptions are relatively constant. Staff recommend providing guidance for private entities on when a roll forward is appropriate and how it should be performed.

    b. For group plans, subsidiaries should be permitted to recognise a charge based on a reasonable allocation of the group charge if the parent prepares consolidated financial statements in accordance with either the IFRS for Private Entities or full IFRSs since accounting for group plans can be complex and may add little informational value if the obligation is shared by many group entities. The basis of allocation should be disclosed.

<u>Question 27.4A</u>

If the Board agrees with the staff recommendation in Issue 27.3 above, does the Board also agree with the staff recommendation that there is no need to provide further simplification by allowing actuarial methods other than the projected unit method to be used for defined benefit accounting?

<u>Question 27.4B</u>

Does the Board agree with the staff recommendation that additional clarification should be added to the ED to state that under defined benefit accounting, an actuarial valuation performed by an outside actuary is not required to be done every year and that guidance should be added on when a roll forward is appropriate and how it should be performed?

<u>Question 27.4C</u>

Does the Board agree with the staff recommendation that additional clarification should be added to the ED to state that subsidiaries are permitted to recognise a charge based on a reasonable allocation of the group charge if the parent prepares consolidated financial statements under either the IFRS for Private Entities or full IFRSs and the basis of allocation is disclosed?

Issue 27.5: Pensions – treat all multi-employer as defined contribution

62. **Reason for revisiting issue.** This issue has not yet been discussed by the Board as staff felt it was more appropriate to discuss the remaining Section 27 issues together.

63. **Comment letters.** Treat all multi-employer plans as defined contribution.

64. **Field tests.** No related comments.

65. **WG recommendation.** Most WG members would encourage the Board to seek simplify the calculation of defined benefit obligations. Some WG members would simplify calculations by treating all multi-employer plans as defined contribution.

66. **Staff comment.** The ED proposes that multi-employer plans be classified as defined contribution or defined benefit based on their terms. However, if sufficient information is not available to use defined benefit accounting, then a private entity can use defined contribution accounting, with disclosure. This requirement is consistent with IAS 19 *Employee Benefits.*

67. **Staff recommendation.** Staff recommend allowing all multi-employer plans to be treated as defined contribution plans with appropriate disclosure (ie the nature of the plan and its funding arrangements) for cost benefit reasons, unless information on the underlying assets and liabilities of the plan is readily available to the entity. Effectively the staff recommendation is just to modify slightly the proposed wording in the ED by replacing 'available' with 'readily available' to clarify that the entity need not make any considerable effort to try to obtain such information if it does not already have the information to hand. The staff recommendation acknowledges that in many cases it is difficult to obtain the information necessary to apply defined benefit accounting in the financial statements of the participating employers (or even to determine the current termination amount, proposed as a simplification in special cases under Issue 27.3) since many multi-employer arrangements effectively share the obligation amongst participating employers without providing detailed information about underlying assets and liabilities. In particular the cost and difficulty of obtaining this information may be significant for smaller private entities.

68. Staff also recommend adding the following based on IAS 19.32A

> There may be a contractual agreement between the multi-employer plan and its participants that determines how the surplus in the plan will be distributed to the participants (or the deficit funded). A participant in a multi-employer plan with such an agreement that accounts for the plan as a defined contribution plan shall recognise the asset or liability that arises from the contractual agreement and the resulting income or expense in profit or loss.

<u>Question 27.5</u>

Does the Board agree with the staff recommendation that the ED should be amended to state that all multi-employer plans should be treated as defined contribution plans with appropriate disclosure unless information on the underlying assets and liabilities of the plan is readily available to the entity?

Issue 27.6 (new): Expected rate of return on assets

69. **Additional staff issue.** Like IAS 19, the ED requires entities to recognise the expected return on assets in profit or loss in measuring the defined benefit obligation. The difference between the actual and expected return on assets forms part of the actuarial gains and losses. Staff believe that private entities should not be required to divide the return on assets into an expected return and an actuarial gain or loss.

70. **Comment letters.** No related comments.

71. **Field tests.** No related comments.

72. **WG recommendation.** Not discussed.

73. **Staff comment.** Both Section 27 of the ED and IAS 19 require entities to recognise in profit or loss an expected return on assets. The difference between the actual and expected return on assets forms part of the actuarial gains and losses.

74. In March 2008, the IASB published for comment a Discussion Paper *Preliminary Views on Amendments to IAS 19 Employee Benefits.* One of the Board's preliminary views in this paper is that entities should not divide the return on assets into an expected return and an actuarial gain or loss. Paragraph 2.15 of the Discussion Paper states "*the Board is concerned that the subjectivity inherent in determining the expected rate of return provides entities with an opportunity to choose a rate with a view to manipulating profit or loss. Accordingly, the Board's preliminary view is that entities should not divide the return on assets into an expected return and an actuarial gain or loss*."

75. **Staff recommendation.** Some users feel that dividing the actual return on plan assets into an expected return and an actuarial gain or loss provides information that is more relevant than a single item representing the actual return. However, staff note that determining the expected rate of return is subjective, and smaller private entities generally have less expertise and may not apply such judgment properly, meaning the number will be less useful for users.

76. For cost-benefit reasons staff propose that entities should not divide the return on assets into an expected return and an actuarial gain or loss. If the Board agrees with the staff recommendation in Issue 27.1 to require immediate recognition of actuarial gains and losses in full during the period, either within profit and loss or in other comprehensive income, then the impact of the staff's proposal here is limited to the presentation of the components of the change in the defined benefit liability. Use of an expected rate only has an impact on the measurement of the defined benefit liability if actuarial gains and losses are deferred.

Question 27.6

Does the Board agree with the staff recommendation that the ED should be amended to state that entities should not divide the return on assets into an expected return and an actuarial gain or loss?

Section 35 Specialised Industries

Issue 35.2 (new): Service concession arrangements (IFRIC 12)

77. **Comment letters.** Some comment letters recommended that the Board review the outstanding interpretations to identify those that address issues that should be covered in the IFRS for Private Entities. This is one such issue.

78. **Staff recommendation.** IFRIC 12 *Service Concession Arrangements* provides guidance on accounting by the concession operator for a service concession arrangement. A number of comment letters said that private entities often are operators of service concession arrangements, and staff enquiries have confirmed that. Staff propose to add the following paragraphs to Section 35 *Specialised Industries*.

35.4 A service concession arrangement is an arrangement whereby a government or other public sector body contracts with a private operator to develop (or upgrade), operate and maintain the grantor's infrastructure assets such as roads, bridges, tunnels, airports, energy distribution networks, prisons or hospitals. In these arrangements, the grantor controls or regulates what services the operator must provide using the assets, to whom, and at what price, and also controls any significant residual interest in the assets at the end of the term of the arrangement.

35.5. There are two principal categories of service concession arrangements:

(a) In one, the operator receives a **financial asset -** an unconditional contractual right to receive a specified or determinable amount of cash or another financial asset from the government in return for constructing or upgrading a public sector asset, and then operating and maintaining the asset for a specified period of time. This category includes guarantees by the government to pay for any shortfall between amounts received from users of the public service and specified or determinable amounts.

(b) In the other, the operator receives an **intangible asset** – a right to charge for use of a public sector asset that it constructs or upgrades and then operates and maintains for a specified period of time. A right to charge users is not an unconditional right to receive cash because the amounts are contingent on the extent to which the public uses the service.

Sometimes, a single contract may contain both types: to the extent that the government has given an unconditional guarantee of payment for the construction of the public sector asset, the operator has a financial asset; to the extent that the operator has to rely on the public using the service in order to obtain payment, the operator has an intangible asset.

Accounting – financial asset model

35.6 The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services. The operator shall measure the financial asset at fair value. Thereafter, it shall follow Section 11 *Financial Assets and Financial Liabilities* in accounting for the financial asset.

Accounting – intangible asset model

35.7 The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. A right to charge users of

the public service is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service. The operator shall initially measure the intangible asset at fair value. Thereafter, it shall follow Section 17 *Intangible Assets other than Goodwill* in accounting for the intangible asset.

Operating revenue

35.8 The operator of a service concession arrangement shall recognise and measure revenue in accordance with Section 22 Revenue for the services it performs.

Question 35.2

Does the Board agree with the staff recommendation that guidance on accounting for service concession arrangements should be added to Section 35 as set out above?

General Issue

Issue G5: Title of the Standard

79. **Reason for revisiting issue.** The title of the standard, currently 'International Financial Reporting Standard for Private Entities', has been an issue throughout the project. In May 2008 the Board tentatively decided:

> The title of the standard should be changed to International Financial Reporting Standard for Private Entities, with private entities defined similarly to the definition of SMEs in the ED. [*IASB Update*, May 2008].

80. Despite the statement that the name change did not change the underlying scope of applicability of the standard, the Board's constituents seem to feel that changing the name to 'private entities' indicated a move away from small and medium-sized entities toward those at the larger-size end of the spectrum of entities without public accountability. This point was made by many participants at the World Standard Setters' meeting on 11-12 September 2008, by members of the Working Group, by representatives of development agencies, and others.

81. **Staff comment.** The Board decided to use SME almost at the outset of the project – after considering the views expressed in responses to the June 2004 Discussion Paper *Preliminary Views on Accounting Standards for Small and Medium-sized Entities.* The Board chose the term SME because it is widely recognised. Since that time, we have used several other titles in addition to SMEs, but all of them have used have defined the types of entities to which the standard would be applicable: "small and medium-sized entities", "non-publicly accountable entities", "private entities". At the same time, we have been saying that each jurisdiction should decide for itself which entities should be within the scope (subject to our two prohibitions of listed entities and financial

institutions). Some respondents have suggested that any title that defines the types of entities to which the standard would be applicable is inevitably inconsistent with saying that this is a jurisdictional decision.

82. An alternative approach to the title would be to describe the nature of the content of the standard (ie the principles) rather than the nature of entities to which the standard would apply. Possible titles on this basis would include “Simplified IFRSs”, “Abridged IFRSs”, and “Concise IFRSs”. Characteristics of the nature of the standards that are captured in these terms include:

    a. The standard is derived from IFRSs,

    b. The standard was developed by the IASB (the sole issuer of IFRSs),

    c. It is shorter than, and not as comprehensive as, IFRSs, and

    d. Some of the requirements differ from those in IFRSs to make it simpler and easier for non-publicly accountable entities to apply.

83. An argument against this approach is that the title could be perceived as implying that the standard is second class to full IFRSs. Staff have been informed that at least one international development agency has strong reservations about a title such as *Simplified IFRSs* because it may be used by entities for which it is not intended and might be viewed sceptically by capital providers. Also, “simplified IFRSs” is a new term whereas “SMEs” and perhaps “private entities” are more globally recognised terms.

84. **Staff recommendation.** As this issue has been re-discussed several times, staff do not want to provide a new recommendation to the Board. Instead staff seek direction on whether or not the standard should:

    - define the types of entities to which the standard would be applicable and, if so, whether the title should be kept as IFRS for Private Entities, changed back to IFRS for SMEs, or changed to something new, for example IFRS for smaller private entities.

    - describe the nature of the content of the standard (i.e. the principles) and, if so whether any Board members have any specific preferences, eg “Simplified IFRSs”, “Concise IFRSs” etc.

Question G5A

Should the title of the standard define the types of entities to which the standard would be applicable or describe the nature of the content of the standard (ie the principles)?

Question G5B

Do Board members have any preferences for a specific title for the Standard?