



---

|         |  |
|---------|--|
| Project | <b>Liabilities – Amendments to IAS 37</b>  |
| Topic   | <b>Measurement of reimbursement rights</b> |

---

## Purpose of paper

1. The purpose of this paper is to help the Board decide whether to add measurement requirements and guidance for reimbursement rights to the revised *IAS 37 Provisions, Contingent Liabilities and Contingent Assets*.

## Staff recommendation

2. The staff recommend that the Board does not add any measurement requirements for reimbursement rights to the revised standard.
3. The staff does however recommend that the standard should state explicitly that the assumptions used to measure a reimbursement right should be consistent with those used to measure the related liability

## Background

### *IAS 37 requirements*

4. At present IAS 37 states that a reimbursement right should be recognised only when it is virtually certain that the reimbursement will be received.
5. IAS 37 does not specify requirements for, or provide any guidance on, measuring reimbursement rights, except for the cap it sets on the amount

---

This paper has been prepared by the technical staff of the IASCF for discussion at a public meeting of the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IASB.

Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRIC or the IASB can make such a determination.

The tentative decisions made by the IASB at its public meetings are reported in *IASB Update*. Official pronouncements of the IASB, including Discussion Papers, Exposure Drafts, IFRSs and Interpretations are published only after it has completed its full due process, including appropriate public consultation and formal voting procedures.

recognised. The amount recognised as a reimbursement right cannot exceed the amount of the related provision.

***Exposure draft proposals***

6. The exposure draft proposed that when an entity has a right to reimbursement for some or all of the economic benefits that will be required to settle a liability it recognises the reimbursement right as an asset if the reimbursement right can be measured reliably. In other words, the ‘virtual certainty’ recognition criterion in the existing IAS 37 is omitted.
7. As the current IAS 37 does not specify how reimbursement rights should be measured, the Board previously argued that it would not be necessary to include any requirements or guidance in the revised standard. Consequently the exposure draft did not propose any measurement requirements or guidance for reimbursement rights.

***Comment letters and subsequent Board discussions***

8. Most respondents agreed or made no comment on the proposed amendments to reimbursement rights in general. However, eight respondents asked the Board to consider including measurement guidance for reimbursement rights in the revised IAS 37. These respondents identified two potential measurement bases for reimbursements – fair value or discounted cash flows (based on the measurement guidance in IAS 37 for the related liability).
9. These respondents were concerned that the absence of guidance in the exposure draft would result in inconsistent measurement of reimbursement rights. They were also concerned about asymmetry in the measurement of closely related assets and liabilities if measurement based on discounted cash flows is not used for reimbursement rights.

10. When the Board first considered these concerns in March 2006, it did not conclude whether to provide additional guidance for reimbursement rights and instead decided to reconsider the issue when it had finalised the measurement guidance for liabilities.

### **Should additional measurement guidance be provided in IAS 37?**

11. The staff think that amending the recognition requirements for reimbursement rights raises questions about measurement of those rights.

#### **Staff analysis**

12. The current IAS 37 provides guidance on accounting for the conditional asset (the reimbursement) rather than the unconditional asset (the right to reimbursement). The ‘virtual certainty’ recognition criterion for reimbursements in the current IAS 37 means that reimbursement rights are recognised only if there is little or no uncertainty about the timing and the amount of the reimbursement to be received. Therefore the absence of measurement guidance in the current IAS 37 for reimbursements is not likely to create application difficulties.
13. The exposure draft, on the other hand, proposes that entities should recognise the unconditional right to reimbursement (as opposed to the reimbursement itself). There is no ‘virtual certainty’ recognition criterion. This implies that any uncertainty about the amount or timing of the reimbursement should be reflected in measurement of that reimbursement right. But guidance on how to reflect this uncertainty is not included in the exposure draft. Nor is the ‘gap’ easily filled by reference to other standards. Specifically:
  - (a) many common reimbursement rights (eg insurance contracts, indemnity clauses) meet the definition of a financial asset in IAS 32 *Financial*

*Instruments: Presentation*.<sup>1</sup> However, IAS 39 *Financial Instruments: Recognition and Measurement* excludes from its scope reimbursement rights relating to liabilities recognised in accordance with IAS 37.<sup>2</sup>

- (b) IFRIC 5 *Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds* provides measurement guidance for specified reimbursement rights. However IFRIC 5 deals with a very specific type of right and, therefore this guidance may not be appropriate in all cases.
14. Arguments for adding measurement requirements for reimbursement rights to the revised standard include:
- (a) Lack of guidance may lead to inconsistencies in measurement. Two entities faced with similar circumstances might decide to use different approaches to measure the reimbursement right and might therefore get different results.
  - (b) In the absence of added guidance there is a possibility that closely related assets and liabilities might not be measured consistently.
  - (c) Any guidance which the Board would develop for this project could be used in the insurance project.
15. Arguments against adding measurement requirements for reimbursement rights to the revised standard include:
- (a) This matter does not directly relate to the Board's existing objectives. The Board previously decided against including measurement guidance for reimbursement rights in the exposure draft because of concerns about scope creep and time constraints.

---

<sup>1</sup> IAS 32.11(c)(i) defines a financial asset as 'a contractual right to receive cash or another financial asset from another entity'.

<sup>2</sup> Paragraphs BC11–BC13 of the Basis for Conclusions accompanying IFRIC 5 *Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation* explains that the IAS 39 scope exclusion was added to ensure consistency in accounting guidance for all reimbursement rights (contractual and non-contractual) because the economic effect of both is the same.

- (b) The Board would have various options to choose from when deciding on measurement requirements. These options include:
- (i) fair value;
  - (ii) the mirror of the liability measurement (the amount the entity would rationally accept at the reporting date in exchange for the reimbursement right); or
  - (iii) the expected present value of the amounts receivable.

The Board could spend considerable time selecting a requirement. Therefore taking it on would risk delaying the project even further.

- (c) This topic may divert attention from more fundamental issues. In most cases, entities recognising liabilities within the scope of IAS 37 will not be recognising reimbursement rights. Constituents' support or opposition to the overall package proposed in the exposure draft is unlikely to be dependent on resolution of this issue.
- (d) The Board could also without specifying the measurement requirements, explicitly state that the assumptions used to estimate a reimbursement right (for example, the assumptions about the possible amounts and timings of future cash flows) should be consistent with those used to estimate the liability it is supposed to offset.
- (e) Many reimbursement rights are likely to arise from insurance contracts. Therefore, the accounting for these rights may be covered by the insurance contract project if it addresses policyholder accounting. However, the staff notes that conclusions on accounting for reimbursements rights arising from insurance contracts may not be appropriate for all reimbursement rights (eg joint and several liabilities).
- (f) Few respondents requested added measurement guidance (only 8 out of 123 comment letters received raised this issue). This might indicate that the lack of guidance would not cause widespread problems in practice nor necessarily lead to inconsistency in the measurement of a reimbursement right and its related liability. The staff thinks it is likely

that entities will use consistent assumptions and techniques when measuring a liability and a related reimbursement right.

**Staff recommendation**

16. The staff think that the arguments for not including measurement requirements for reimbursement rights in the revised IAS 37 outweigh the arguments for including them.
17. However, the staff think that the Board should, without specifying the measurement requirements, state that the assumptions used to measure a reimbursement right should be consistent with those used to measure the related liability as pointed out in paragraph 15 (d).

**Staff recommendation and question for the Board**

The staff recommend not specifying a measurement objective for reimbursement rights in IAS 37. Do you agree?

However, the staff recommend that the standard should state explicitly that the assumptions used to measure a reimbursement right should be consistent with those used to measure the related liability. Do you agree?