Topic **IASB Chairman - Quarterly Review**

1. This is my last report to the IFRS Advisory Council as Chairman of the IASB. When I assumed this role ten years ago I am sure that few foresaw that by the end of 2010 IFRSs would be so widely adopted. Nor did many anticipate that in the same period such a new, and small, organisation would be able to manage such an extensive agenda and deliver so many improvements to financial reporting.

2. This report provides an overview of the projects on our technical agenda. It is an agenda that has become much smaller over the past two years as the Board has made it a priority to focus on completing projects responding to matters raised during the financial crisis and on completing the IASB-FASB Memorandum of Understanding (MoU) projects:

   (a) The short-term projects identified for action in the MoU have been completed or are close to completion.

   (b) Of the longer-term projects, only three of the priority convergence projects remain for which the boards have yet to finalise the technical decisions—financial instruments, revenue recognition and leasing.

3. Most of the short-term projects required one of the boards to revise its requirements to align them with those of the other board. Other projects, such as share-based payment, required both boards to issue revised standards.

	Project	Board	Status	Milestone
1	**Share-based payments**	Both	Completed	Substantially common standards issued in 2004.
2	**Segment reporting**	IASB	Completed	IFRS 8 *Operating Segments* issued in 2006.
3	**Non-monetary assets**	FASB	Completed	FASB converged on the treatment of certain non-monetary exchanges to require recognition at fair value unless the transaction lacks commercial substance in SFAS 153 *Nonmonetary Assets* issued in 2004.
4	**Inventory accounting**	FASB	Completed	FASB converged on the treatment of excess freight and spoilage in SFAS 151 *Inventory Costs* issued in 2004.
5	**Accounting changes**	FASB	Completed	FASB converged on the treatment of voluntary changes in accounting policy by requiring retrospective application in SFAS 154 *Accounting Changes and Error Corrections* issued in 2005.
6	**Fair value option**	FASB	Completed	SFAS 159 *The Fair Value Option for Financial Assets and Financial Liabilities* issued in 2007, introducing the fair value option into US GAAP.
7	**Borrowing costs**	IASB	Completed	Revised IAS 23 *Borrowing Costs* issued in 2007.
8	**Research Costs**	FASB	Completed	SFAS 141R *Business Combinations* issued in 2008, amending the accounting for acquired R&D.
9	**Non-controlling interests**	FASB	Completed	SFAS 160 *Noncontrolling Interests in Consolidated Financial Statements* issued in 2008, eliminating the use of mezzanine presentation of non-controlling interests.
10	**Joint ventures**	IASB	Completed	IFRS 11 *Joint Arrangements* issued in May 2011.
11	**Income tax**	Both	Reassessed as a lower priority project. No immediate action.	IASB exposure draft published in 2009.
12	**Investment properties**	FASB	In progress.	The FASB plans to publish an exposure draft in July to propose bringing US GAAP closer to IFRSs.

4. The boards also have a project in progress to develop a joint *Conceptual Framework for Financial Reporting*. In 2010 the boards published chapters on objectives and qualitative characteristics.

5. With the exception of the three remaining priority MoU projects, the following schedule details the progress of the IASB and the FASB MoU projects:

	Project	Status	Milestone
1	**Business combinations**	Completed	Joint requirements for business combination accounting and non-controlling interests issued in 2008—IFRS 3 *Business Combinations* and amended IAS 27 *Consolidated and Separate Financial Statements*.
2	**Derecognition**	Completed	Each board has introduced reforms substantially aligning the disclosure requirements, and as a result US GAAP has moved closer to IFRSs.
3	**Consolidated financial statements** (including disclosure about off balance sheet risks)	Completed	IFRS 10 *Consolidated Financial Statements* and IFRS 12 *Disclosure of Interests in Other Entities* issued in May 2011.
4	**Fair value measurement**	Completed	SFAS 157 *Fair Value Measurements* issued in 2006. IFRS 13 *Fair Value Measurement* issued in May 2011.
5	**Post-employment benefits**	Completed	Amendments to IAS 19 *Employee Benefits* issued in June 2011.
6	**Financial statement presentation—other comprehensive income**	IFRS and US GAAP amendments issued in June 2011. Further consideration on other aspects of financial statement presentation are not expected before December 2011.	Amendments to IFRSs and US GAAP for presentation of other comprehensive income issued in June 2011.
7	**Financial instruments with the characteristics of equity**	Reassessed as a lower priority project. Further consideration is not expected before December 2011.	Joint discussion paper published in 2008.
8	**Intangible assets**	The IASB decided not to proceed with the project, but will reconsider it when it sets its new agenda.	The IASB considered an agenda proposal to add a project on intangible assets in December 2007.

6. Completing the MoU projects is an important step to having IFRSs adopted by the US. The more we can reduce the differences between IFRSs and US GAAP the easier it will be for US entities to adopt IFRSs.

7. Last month the SEC released an update to its work plan, outlining how IFRSs could be incorporated into US GAAP. The SEC staff have been making a careful and thorough assessment of the different ways that IFRSs can be incorporated into the US legal system. The reports continue to be exploratory and open to different approaches. We expect the SEC to provide much more clarity about US adoption towards the end of the year.

8. The sections that follow outline the main developments in the projects on the agenda.

The financial crisis projects

9. The Board has put considerable effort into addressing concerns raised by users, preparers, politicians, regulators and other financial market participants about:

   (a) the complexity of IAS 39 *Financial Instruments: Recognition and Measurement*;

   (b) the effectiveness of the incurred loss model for loan provisions;

   (c) off balance sheet risks, in particular those related to securitisations (derecognition) and special purpose vehicles (consolidation); and

   (d) fair value measurement of assets especially when markets became illiquid.

Financial instruments

10. The boards' efforts to improve our requirements and to reach a common solution have been complicated by differing imperatives that pushed our development timetables out of alignment. In particular, the IASB has been replacing its financial instrument requirements in a phased approach, whereas the FASB developed a single proposal. Those differing development timetables and other factors have contributed to the boards reaching different conclusions on some important technical issues.

11. Our broad strategy for addressing those differences remains the same—each board has been publishing its proposals and at the same time inviting comment on those of the other board, as a way of giving interested parties the opportunity to compare and assess the relative merits of both boards' proposals. We consider together the comment letters and other responses that we receive, in an effort to reconcile our differences in ways that foster improvement and convergence. For some parts of the project—impairment and offsetting—the boards have been able to align their timetables and work together, developing joint exposure drafts.

Classification and measurement

12. IFRS 9 *Financial Instruments* has been developed in phases. The classification and measurement and derecognition requirements have already been endorsed in many jurisdictions. However, we continue to receive requests, particularly from some European organisations, to reopen aspects of IFRS 9. Some parties would like the IASB to consider reintroducing bifurcation of financial assets and reintroducing some notion of 'available-for-sale' financial assets, even though these changes were strongly supported when we developed IFRS 9. On the other hand, many organisations, including some European ones, have told us *not* to reopen the classification and measurement parts of IFRS 9.

13. We will continue to receive these competing pressures until the FASB has finished its deliberations on classification and measurement. The FASB has already stated publicly that it believes that amortised cost is an appropriate measurement basis for some financial instruments. However, the FASB has still to determine how many classification categories it will require or whether it will retain its existing bifurcation rules.

14. Once the FASB has made its decisions about classification and measurement, we will assess how best to expose the FASB's final conclusions to seek views on whether the Board will need to consider how, or indeed if, it should bridge or reconcile any differences between IFRS 9 and US GAAP. Any such assessment now would be premature because the FASB has not developed its model fully.

Impairment

15. In late January the Board published, jointly with the FASB, a supplement to the December 2009 exposure draft. The supplement presented an impairment model that the boards believed would enable them to satisfy at least part of their individual objectives for impairment accounting while achieving a common solution to impairment.

16. The boards received 212 comment letters and views were mixed. Many respondents would prefer the IASB's simplified proposals—seeing the addition of a floor (which came from the FASB model) as a complication. Others prefer aspects of the US model (which recognised expected losses for the 'foreseeable future'). In May the boards set up a task force of staff and board members to work on the model. Both boards recognise the importance of this phase of the financial instruments model and the need to reach a common solution. The boards discussed a potential model in June.

Hedge accounting

17. In December 2010 the Board published proposals to revise hedge accounting, for both financial and non-financial exposures. Comments were due by 9 March. During the comment period, staff and Board members undertook outreach activities in five continents, meeting over 2,500 people in small group meetings and discussion forums. The Board received 233 comment letters, a summary of which was presented to the Board in March.

18. There was strong support for the proposals, with respondents welcoming the Board's approach, namely to address hedge accounting comprehensively. They also agree with the principle-based approach proposed in the exposure draft, with many commenting that the proposal would resolve many of today's practice problems in applying IAS 39 *Financial Instruments: Recognition and Measurement*.

19. The exposure draft published in December was concerned with general hedge accounting. It did not address portfolio hedges. In February a financial

instruments expert from a major accounting firm was seconded to the hedge accounting team, to work on proposals for portfolio hedges. The Board resumed its public discussion of portfolio hedges in May and expects to develop more fully its proposals related to portfolio hedging before it finalises the more general hedging requirements. We therefore expect to publish an exposure draft for portfolio hedging later this year.

Balance sheet netting of derivatives and other financial instruments

20. In late January the boards published a joint exposure draft proposing changes to IFRSs and US GAAP that would align the reporting of offsetting financial assets and liabilities. The boards received 162 comment letters. Views were mixed. There is broader support for the proposals from those applying or moving to IFRSs than from those applying US GAAP. Some respondents would prefer us to allow more netting (which would be closer to current US GAAP) while others think it is better not to allow netting except in restricted circumstances. The project itself is not difficult from a technical accounting perspective, but the financial reporting consequences of reaching a shared solution with the FASB will be significant for many entities.

Consolidation

21. On 13 May 2011 the IASB issued IFRS 10 *Consolidated Financial Statements* and IFRS 12 *Disclosure of Interests in Other Entities*. IFRS 10 provides a single consolidation model that identifies control as the basis for consolidation for all types of entities. IFRS 10 replaces IAS 27 *Consolidated and Separate Financial Statements* and SIC-12 *Consolidation— Special Purpose Entities*. IFRS 12 combines, enhances and replaces the disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities. As a consequence of these new IFRSs, the IASB also issued amended and retitled IAS 27 *Separate Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures*. The new requirements are effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

22. The FASB is preparing to expose the principal-agent sections of the IFRS 10 model. If the FASB finalises the proposals, some small differences will remain in relation to voting interest entities. US GAAP will continue to allow some entities controlled by votes not to be consolidated. The FASB chose not to implement the full IFRS model now, but to review application of IFRS 10. Despite this gap, the changes made by both boards align the recognition and disclosure requirements for the areas that caused the greatest concern during the financial crisis.

Fair value measurement

23. On 13 May 2011 the IASB issued IFRS 13 *Fair Value Measurement*. IFRS 13 defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements.

24. As a result, the definitions of fair value are the same in IFRSs and US GAAP. IFRS 13 (like US GAAP) also provides guidance on measuring fair value when markets are illiquid. IFRS 13 does not, and the FASB standard did not, introduce any new requirements about when to use fair value. IFRS 13 is concerned only with how to measure fair value when it is required by an IFRS. The new requirements, like those of IFRS 10 and IFRS 12 are effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

Other major projects

25. In addition to the financial crisis-related projects, the Board is working on three major projects. Revenue recognition and leases are MoU projects being developed jointly with the FASB. Insurance contracts is not in the MoU, but the IASB has been working with the FASB with the goal of developing common requirements.

MoU projects

Revenue recognition

26. The IASB and FASB published a joint discussion paper in December 2008 that proposed a single revenue recognition model built on the principle that an entity should recognise revenue when it satisfies its performance obligations in a contract by transferring goods or services to a customer. That principle is similar to many existing requirements. However, the boards think that clarifying that principle and applying it consistently to all contracts with customers will improve the comparability and understandability of revenue for users of financial statements.

27. The project is critical to both the FASB and the IASB. US GAAP has a wide range of detailed industry-specific requirements. The IASB has very general requirements that cause preparers to rely on US GAAP for specific guidance. The project is intended to reduce the FASB's detailed guidance to consistent principles and to remove the need for IFRS users to refer to US GAAP.

28. The comment period closed on 22 October 2010 and the Boards received 971 comment letters (of which 247 are 'form' letters from entities in the construction industry). The boards held round tables in London, San Francisco, Norwalk and Kuala Lumpur.

29. In December 2010 the boards began discussing the comments received on the exposure draft. The comment letters and round-table discussions showed strong support for the project generally. It is clear that there were two main issues to reconsider:

    (a) separating a contract; and

    (b) determining when goods and services are transferred to a customer.

30. The boards acknowledged that they needed to explain more clearly the principles behind these fundamental parts of the revenue recognition model, to ensure that the standard will be capable of being applied consistently across a wide range of contracts. Although many other issues were raised in the letters,

the boards noted that most of these were likely to be capable of being addressed by simplifying the proposals so that the requirements are more operational.

31. In June the boards decided to re-expose their revised proposals for a common revenue recognition standard. Re-exposing the revised proposals will provide interested parties with an opportunity to comment on revisions the boards have undertaken since the publication of an exposure draft on revenue recognition in June 2010.

32. It was the unanimous view of the boards that while there was no formal due process requirement to re-expose the proposals it was appropriate to go beyond established due process given the importance of the revenue number to all companies and the need to take all possible steps to avoid unintended consequences.

33. Consequently, the boards intend to re-expose their work in the third quarter of 2011 for a comment period of 120 days.

Leases

34. The boards included a leases project in the 2006 MoU because both boards' highly similar standards need significant improvement. The objective of this project is to develop common lease accounting requirements that would improve financial reporting by ensuring that all assets and liabilities arising from lease contracts are recognised in the statement of financial position. The boards published a joint discussion paper in March 2009.

35. In August 2010 the boards published a joint exposure draft, proposing to bring lease obligations and the related asset onto the balance sheet of lessees. The comment period closed on 15 December and we have received 760 comment letters. The boards held round-table meetings in London, Chicago, Norwalk, and Hong Kong.

36. In response to the comments received the boards have agreed on a revised definition of a lease to avoid catching what are widely perceived to be service agreements. The boards also believe the changes from the exposure draft they

are proposing address concerns raised in relation to contingent rentals and renewal options.

37. In June the boards considered the two remaining important parts of the project:

(a) Lessees

The boards have decided that, as a principle, the (right of use) asset and related lease obligation should be recognised by a lessee. The boards had been considering different income recognition models for some, generally shorter-term, leases. However, the boards have decided not to pursue that approach. Instead, the boards have assessed whether an exception should be introduced to simplify the requirements for some leases (either because they are for a relatively short period or because the integrated services reduce the usefulness of separating a finance component). The boards have decided that an exception be permitted for leases of 12 months or less.

(b) Lessors

The boards have tentatively decided not to pursue the performance obligation approach, a method that was not well received. In May the boards were split, with a majority of the IASB preferring a partial derecognition model and a majority of the FASB preferring to retain the basic approach used today—with lessors distinguishing between finance (capital) leases and operating leases. The boards are developing a partial derecognition model and will then decide whether to keep the present basic requirements for lessor accounting or to make a change which attracted considerable support from our constituents. This remains the last major issue to be resolved for the project.

38. Once the boards have addressed the lessor matter they will be in a position to assess whether to re-expose the proposals. If the boards conclude that re-exposure is not necessary at this stage, they intend to develop a review draft of the new standard (including application guidance and a basis for conclusions), which will be:

(a) made generally available, via the boards' websites, for interested parties to review;

(b) used as the basis for outreach with parties that are most affected by the proposed new requirements; and

(c) subjected to a detailed drafting review with selected parties.

39. The boards will consider the feedback that they receive from these steps to assess whether they can proceed to finalise the standard, whether additional work is required or whether re-exposure is necessary at that point.

Financial statement presentation

40. On 16 June the Board issued amendments to IAS 1 *Financial Statement Presentation.* These amendments improve how we present components of other comprehensive income. The FASB issued equivalent requirements on the same day. Although the improvements to IAS 1 are important they are not as significant as the improvements to US GAAP—the US will now have comprehensive income presented in either one statement or two consecutive statements.

Post-retirement benefits

41. On 16 June the Board issued amendments to IAS 19 *Employee Benefits*. The amendments will improve the recognition and disclosure requirements for defined benefit plans. The new requirements are effective for annual periods beginning on or after 1 January 2013, with earlier application permitted. This completed one of our narrower-scope MoU projects.

Joint ventures

42. The Board delayed finalising its new standard on joint arrangements to ensure that the wording was aligned with the new *Consolidations* IFRS. In May 2011 the IASB issued IFRS 11 *Joint Arrangements*, which supersedes IAS 31 *Interests in Joint Ventures* and SIC-13—*Jointly Controlled Entities–Non-monetary Contributions by Venturers*. The new requirements are effective

for annual periods beginning on or after 1 January 2013, with earlier application permitted. This completed another of our narrower-scope MoU projects.

Non-MoU projects

Insurance contracts

43. IFRSs lack specific accounting requirements for insurance contracts. The IASB has had a major project on its agenda for many years to remedy that deficiency. In 2007 the IASB published a discussion paper, *Preliminary Views on Insurance Contracts*, and has been developing proposals on the basis of that discussion paper and in the light of comments received on it. In October 2008 the IASB and FASB agreed to work on the project together. The IASB published an exposure draft *Insurance Contracts* on 30 June 2010, which the FASB published as a discussion document in September 2010.

44. The IASB received 247 comment letters and the FASB received 74 comment letters. The boards held public round tables in London, Norwalk and Tokyo in December.

45. The boards have been redeliberating the issues since February. Unfortunately, the boards have reached different decisions on several aspects of the project. We will need to return to those matters if we are to develop common solutions

46. There are two other challenges. The IASB has already published an exposure draft whereas the FASB has published only a discussion paper. The boards will need to assess how best to align the timetables so that the outcome is identical standards. Although having our due process steps out of step does not prevent us from developing high quality solutions, as the fair value measurement project demonstrates, it does make it more difficult.

47. The other challenge is the relationship between the insurance contracts project and the financial instruments project. The IASB will need to ensure that the insurance contracts IFRS and the financial instruments requirements (IFRS 9) work together.

Other projects

Annual Improvements

48. The Board will be publishing the next round of annual improvements before the end of June. The current cycle contains seven proposed amendments affecting five IFRSs. Each amendment was developed for the Board by the IFRS Interpretations Committee. The Committee's analysis and recommendation were discussed by the Board. In each case the Board decided to publish an improvement proposal.

49. The Committee recommended rejecting many requests for annual improvements. In each such case the Board reviewed the recommendation. In all cases the Board concurred with the Committee.

50. This batch of proposed improvements was originally scheduled to be published in September 2010. However, the Board delayed publication because of the importance of completing other projects and because the annual improvements criteria were being reviewed.

Investment entities

51. In July the Board will publish an exposure draft proposing an exception to consolidation for investment entities. These entities manage and report their investments using fair value and, along with some users, argue that they should report their investments at fair value even when they control another entity. Such an exception has been part of Canadian and US GAAP for many years. The FASB will publish an equivalent exposure draft at the same time, in an effort to simplify the criteria and align the requirements with IFRSs.

Effective dates and transition

52. In October last year we published, with the FASB, a *Request for Views* seeking views on ways in which we can reduce the costs of applying new requirements. Our consultation focuses on three areas:

(a) the effective dates of new requirements—giving entities sufficient time to prepare and also considering whether entities prefer to deal with many changes at once or spread over two or more periods.

(b) early adoption—should we allow early adoption?

(c) transition—do we require entities to go back and apply the new accounting for the comparative periods on which they report (our normal approach) or should we allow more concessions, because of the larger than normal number of changes, to reduce the cost of the change?

53. The Board received 149 comment letters, a summary of which the Board discussed in March. In the last few months the two boards have been surveying users, seeking their views on whether, or how, to sequence effective dates for the major MoU projects. The Board expects to consider that additional information in July.

54. The nature of this consultation has changed since the request for views was released last October. The IASB recently issued four new IFRSs for which it set an effective date of 1 January 2013. The Board considered the responses it had received to the *Request for Views* before it set the dates. Those standards are now outside the current consultation. At the time the consultation began the Board was also aiming to complete several major MoU projects by the end of June 2011. It is clear that the projects will be completed over a longer period than was envisaged last October. Although the Board will still need to co-ordinate effective dates and other transitional provisions, the challenge of dealing with several major projects being completed at the same time is less.

Future agenda

55. At this meeting you have a draft of the *Request for Views* on the future agenda of the IASB. This draft reflects views the Board received from the Advisory Council when it discussed an earlier draft in February meeting. The Trustees will consider this draft when they meet in mid-July.

56. Once the Board has considered comments provided by Trustees and members of the Advisory Council, it plans to publish the consultative document in late July with a comment period of at least 120 days. The decision to publish in July, rather than at some earlier date, is to make it clear that the consultation belongs to the new Board.

57. We have a web page dedicated to this consultation, which includes links to the report sent to the Board by the Advisory Council and to information about the agenda-setting criteria. The World Standard-setters Conference in September includes a session focusing on the agenda consultation. We are also planning to have public round tables after the comment period has ended.