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Project **Annual Improvements—2010-2012 cycle**

Topic **IFRS 13 Fair Value Measurement —Short-term receivables and payables**

Introduction

1. In May 2011, the Board published IFRS 13 *Fair Value Measurement*. A constituent requested that we clarify the intention of a consequential amendment to IFRS 9 *Financial Instruments* (issued October 2010) that resulted from IFRS 13.

Purpose of the paper

2. This paper:
   (a) provides an explanation of the matter raised by the constituent;
   (b) describes two different views about how to deal with the matter;
   (c) assesses the issue against the annual improvements criteria; and
   (d) asks the Board which view it prefers.
3. This paper makes a proposal for an amendment to be included in the annual improvements process. Due to the expected timing of the next annual improvements ED (December 2011) we are bringing this issue directly to the Board for its consideration. The view preferred by the Board will be included in the next ED.

Matter raised by the constituent

4. The constituent asks what the intention of the Board was when it deleted paragraph B5.4.12 of IFRS 9 through the amendment in paragraph D38 of IFRS 13. Paragraph B5.4.12 stated [emphasis added]:

> B5.4.12 In applying discounted cash flow analysis, an entity uses one or more discount rates equal to the prevailing rates of return for financial instruments having substantially the same terms and characteristics, including the credit quality of the instrument, the remaining term over which the contractual interest rate is fixed, the remaining term to repayment of the principal and the currency in which payments are to be made. **Short-term receivables and payables with no stated interest rate may be measured at the original invoice amount if the effect of discounting is immaterial.**

5. This paragraph contains a practical expedient to measure short-term receivables and payables with no stated interest rate at invoice amounts without discounting.

6. Furthermore, the Board retained paragraph 29 (a) of IFRS 7 *Financial Instruments: Disclosures*, which states:

> 29 Disclosures of fair value are not required:
>
> (a) when the carrying amount is a reasonable approximation of fair value, for example, for financial instruments such as short-term trade receivables and payables; […]

7. The question that has been raised with us is whether, by deleting paragraph B5.4.12 in IFRS 9 and retaining paragraph 29 (a) of IFRS 7, the Board intentionally decided to remove the practical expedient.

Views on the matter

View A

8. The deletion of the paragraph did not aim to change practice in the measurement of short-term receivables and payables with no stated interest rate. However, supporters of this view think that this deletion could have unintended consequences in that it might be perceived that guidance has changed. One such consequence that has been highlighted to us is that without this paragraph some take the view that entities that do not discount short-term receivables and

payables on the basis that doing so would have an immaterial effect, nonetheless are not in compliance with the standard and therefore have an 'immaterial error' that would need to be recorded and reported as such during the audit process. We are informed, however, that reinstating the explicit relief would remove this concern.

9. Supporters of this view recommend to the Board to reinstate paragraph B5.4.12 in IFRS 9. Appendix A to this paper contains proposed wording for an amendment to reflect View A. If the Board agrees with View A, the same amendment would be made to reinstate paragraph AG79 of IAS 39 *Financial Instruments: Recognition and Measurement*.

View B

10. The deletion of paragraph B5.4.12 of IFRS 9 should not cause any change in current practice because:

    (a) the guidance provided in it is redundant because IFRS 13 contains guidance for using present value techniques (including discounted cash flow methods); and

    (b) the consideration of materiality should be present when entities decide whether short-term non-interest bearing receivables and payables need to be discounted (ie the practical expedient would not apply if the effect of discounting short-term non-interest bearing receivables and payables is material).

11. As a result, the deletion did not intend to change the practical expedient to measure short-term receivables and payables with no stated interest rate at invoice amounts without discounting when the effect of not discounting is immaterial. Instead, the deletion had been made on the basis that the guidance was no longer needed in IFRS 9 because it had been incorporated into IFRS 13 and materiality is a concept dealt in IAS 1 *Presentation of Financial Statements*. In effect, IAS 1 already contains such a practical expedient.

12. The exposure draft *Fair Value Measurement* published in May 2009 proposed to delete this paragraph in IAS 39, however only one constituent at that time expressed opposition to this deletion.

13. The supporters of View B recommend not to reinstate paragraph B5.4.12 in IFRS 9 but to add a paragraph in the Basis for Conclusions of IFRS 13 providing rationale to support the deletion of that paragraph in IFRS 9.

14. Appendix B to this paper contains proposed wording for the amendment to the Basis for Conclusions of IFRS 13 to reflect View B.

Annual improvements criteria assessment

15. We have assessed the proposed amendment against the enhanced annual improvements criteria, which is reproduced in full below. In planning whether an issue should be addressed by amending IFRSs within the annual improvements project, the IASB assesses the issue against the following criteria. All the criteria (a)-(d) must be met to qualify for inclusion in annual improvements:

New annual improvements criteria	Staff assessment of the proposed amendment
(a) The proposed amendment has one or both of the following characteristics: (i) clarifying—the proposed amendment would improve IFRSs by: • clarifying unclear wording in existing IFRSs, or • providing guidance where an absence of guidance is causing concern. A clarifying amendment maintains consistency with the existing principles within the applicable IFRSs. It does not propose a new principle, or a change to an existing principle. (ii) correcting—the proposed amendment would improve IFRSs by: • resolving a conflict between existing requirements of IFRSs and providing	(a) Yes. The proposed amendment would clarify that discounting of short-term receivables and payables is not required if the effect of discounting is not material. Either adding back the requirements that were removed (View A) or adding an explanatory paragraph in the Basis for Conclusions of IFRS 13 (View B) would re-establish clarity in the requirements.

a straightforward rationale for which existing requirement should be applied, or • addressing an oversight or relatively minor unintended consequence of the existing requirements of IFRSs. A correcting amendment does not propose a new principle or a change to an existing principle, but may create an exception from an existing principle.	
(b) The proposed amendment is well defined and sufficiently narrow in scope such that the consequences of the proposed change have been considered.	(b) Yes. We believe that the proposed amendment is well defined and is sufficiently narrow in scope.
(c) It is probable that the IASB will reach conclusion on the issue on a timely basis. Inability to reach conclusion on a timely basis may indicate that the cause of the issue is more fundamental than can be resolved within annual improvements.	(c) Yes. We think the IASB could reach a conclusion on this issue on a timely basis because this deals with an amendment that is well defined.
(d) If the proposed amendment would amend IFRSs that are the subject of a current or planned IASB project, there must be a need to make the amendment sooner than the project would.	(d) No, the proposed amendment is not related to any current or planned IASB project.

16. Following the analysis in the table above, in our opinion, the proposed amendment satisfies the annual improvements criteria.

17. We think that either amendment (View A or View B) will achieve the intention of clarifying the circumstances in which short-term payables and receivables should be discounted. However, we think that View A will more effectively remove all the concerns raised to us as detailed in paragraphs 7 and 8 of this paper. As a result, we recommend to the Board to deal with the matter in accordance with View A.

Questions for the Board
Does the Board agree with the staff's recommendation in paragraph 17?

Appendix A—View A: Proposed amendment to IFRS 13[1]

Paragraph D38 is amended and paragraph D38A is added (new text is underlined).

D38A After paragraph B5.2.2A, a heading and paragraph B5.2.2B is added as follows:

Short-term receivables and payables with no stated interest rate

B5.2.2B In applying discounted cash flow analysis, an entity uses one or more discount rates equal to the prevailing rates of return for financial instruments having substantially the same terms and characteristics, including the credit quality of the instrument, the remaining term over which the contractual interest rate is fixed, the remaining term to repayment of the principal and the currency in which payments are to be made. Short-term receivables and payables with no stated interest rate may be measured at the original invoice amount if the effect of discounting is immaterial.

Effective date and transition

In Appendix C, paragraph C4 is added as follows:

C4 *Improvements to IFRSs* issued in [date] added paragraph D38A. An entity shall apply that amendment when it applies this IFRS.

Basis for Conclusions on proposed amendment to IFRS 13

Short-term receivables and payables with no stated interest rate

BC1 After issuing IFRS 13 the Board was made aware that an amendment to IFRS 9 that resulted in the deletion of paragraph B5.4.12 might be perceived as removing the ability to apply a practical expedient to measure short-term receivables and payables with no stated interest rate at invoice amounts without discounting when the effect of discounting is immaterial. The Board did not intend to change practice in the measurement of those short-term receivables and payables, but understands that constituents might perceive the deletion as removing the ability to apply the practical expedient. Consequently, the Board proposes to reincorporate paragraph B5.4.12 into IFRS 9.

[1] This appendix only shows the proposed amendment to reinstate paragraph B5.4.12 in IFRS 9. An identical amendment would be also proposed to reinstate paragraph AG79 in IAS 39.

Appendix B—View B: Proposed amendment to the Basis for Conclusions of IFRS 13[2]

Paragraph BC138A and its related heading are added as follows:

Short-term receivables and payables with no stated interest rate

BC138A After issuing IFRS 13 the Board was made aware that an amendment to IFRS 9 that resulted in the deletion of paragraph B5.4.12 might be perceived as removing the ability to apply a practical expedient to measure short-term receivables and payables with no stated interest rate at invoice amounts without discounting when the effect of discounting is immaterial. The Board did not intend to change practice in the measurement of those short-term receivables and payables. In determining whether to retain paragraph B5.4.12 in IFRS 9, the Board concluded that the paragraph was no longer needed for two reasons: (a) IFRS 13 contains guidance for using present value techniques and (b) IAS 1 *Presentation of Financial Statements* addresses materiality, effectively providing such a practical expedient.

[2] The final wording of this amendment would also include the reference to the paragraph in IAS 39 that was deleted by IFRS 13.