IFRIC Update

From the IFRS Interpretations Committee

March 2012

Welcome to IFRIC Update

IFRIC Update *is the newsletter of the IFRS Interpretations Committee and is published as a convenience to the IASB's constituents. All conclusions reported are tentative and may be changed or modified at future IFRS Interpretations Committee meetings.*

Decisions become final only after the Interpretations Committee has taken a formal vote on an Interpretation or Draft Interpretation, which is confirmed by the IASB.

The Interpretations Committee met in London on **13 and 14 March 2012**, when it discussed:

- Current agenda:
  - IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*—Levies charged for participation in a specific market (date of recognition of a liability)
  - IFRIC 12 *Service Concession Arrangements*— Payments made by an operator in a service concession arrangement
  - IAS 28 *Investments in Associates and Joint Ventures*—Application of the equity method when an associate's equity changes outside comprehensive income
- IFRS Interpretations Committee agenda decisions
- Issues considered for *Annual Improvements*
- IFRS Interpretations Committee work in progress
- Trustees' review of the efficiency and effectiveness of the IFRS Interpretations Committee

Contact us

IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH
United Kingdom

Tel: +44 (0)20 7246 6410
Fax: +44 (0)20 7246 6411
E-mail: **ifric@ifrs.org**
Website: **www.ifrs.org**

Future IFRS Interpretations Committee meetings

The next meetings are:
15 and 16 May 2012
10 and 11 July 2012
18 and 19 September 2012
13 and 14 November 2012
Meeting dates, tentative agendas and additional details about the next meeting will be posted to the IASB **website** before the meeting. Instructions for submitting requests for Interpretations are given on the IASB website **here**.

Archive of IFRS Interpretations Committee Newsletter

For archived copies of past issues of IFRIC Update **click here**.

Current agenda

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

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*—Levies charged for participation in a specific market (date of recognition of a liability)

The Interpretations Committee received a request to clarify whether, under certain circumstances, IFRIC 6 *Liabilities arising from participating in a specific market—Waste Electrical and Electronic Equipment* should be applied by analogy to identify the obligating event that gives rise to a liability for other levies charged by public authorities on entities that participate in a specific market. The concern relates to when the liability to pay a levy should be recognised and to the definition of a present obligation in IAS 37.

At the March 2012 meeting, the Committee discussed a draft interpretation presented by the staff. The Committee confirmed its previous decision to develop an interpretation based on the principles identified by the Committee (see January 2012 IFRIC *Update*). The interpretation will address the accounting for levies other than income taxes that are within the scope of IAS 12 *Income Taxes*. The Committee decided to limit the scope of the interpretation to levies that are non-exchange transactions (ie transactions in which the entity paying the levy does not receive any specific asset directly in exchange for the payment of the levy). The Committee decided not to address in the interpretation the accounting for levies subject to a revenue threshold, because the Committee could not reach consensus on that topic. The staff will present a revised draft interpretation for the Committee's approval at the May 2012 Committee meeting.

IFRIC 12 *Service Concession Arrangements*—Payments made by an operator in a service concession arrangement

The Interpretations Committee received a request to address an issue that is related to contractual payments to be made by an operator under a service concession arrangement within the scope of IFRIC 12. Specifically, the submitter requested that the Committee should clarify in what circumstances (if any) those payments should:

a. be recognised at the start of the concession as an asset with a liability to make the related payments; or
b. be accounted for as executory in nature, to be recognised over the term of the concession arrangement.

This issue was previously discussed by the Committee at its November 2011 and January 2012 meetings.

At this meeting, the Committee tentatively decided that:

- if the concession fee arrangement gives the operator a right to a good or service that is distinct from the service concession arrangement, the operator should account for that distinct good or service in accordance with the applicable IFRS;
- when the concession payments are linked to the right of use of a tangible asset, judgement should be used to determine whether the operator obtains control of the right of use of the asset. If the operator controls the right of use the arrangement would be considered to be an embedded lease within the scope of IAS 17 *Leases* (as discussed by the Committee in the November 2011 Committee meeting);
- when the payments are linked to the right of use of a tangible asset, but the arrangement does not represent an embedded lease, the payment should be analysed in the same way as a concession fee (as discussed by the Committee in the November 2011 Committee meeting); and
- if the concession fee arrangement does not give the operator a right to a distinct good or service or a right of use that meets the definition of a lease, the type of service concession arrangement should determine the accounting for the contractual payments to be made by the operator to the grantor:
    - if the service concession results in the operator having a contractual right to receive cash from only the grantor (ie the financial asset model in IFRIC 12 applies), then the concession payment is an adjustment to the overall revenue consideration;
    - if the service concession arrangement results in the operator having only a right to charge users of the public service (ie the intangible asset model in IFRIC 12 applies), then the concession payment represents consideration for the concession right (ie part of the cost of the intangible asset recognised); and
    - If the operator has both a right to charge users of the public service and a contractual right to receive cash from the grantor (eg the in-substance guarantee from the grantor for the operator's services), then the amount of the contractual right to receive cash from the grantor needs to be compared with the fair value of the operator's services to help determine whether the concession payment represents an adjustment to the

overall revenue consideration or consideration for the concession right intangible asset.

The Committee was concerned about delaying any consideration of variable concession fees until the Leases project has been completed. Consequently, the Committee asked the staff to analyse the issue of variable concession fees, and to recommend the appropriate accounting for such fees taking into consideration the principles currently contained in the exposure draft for Leases as the basis for this analysis.

The Committee also asked the staff to prepare a draft amendment to IFRIC 12 to incorporate the above principles discussed by the Committee, which would also include the staff's recommendations relating to variable payments.

The staff's analysis on the accounting for variable concession fees, as well as the draft amendment, will be considered by the Committee at a future meeting.

IAS 28 *Investments in Associates and Joint Ventures*—Application of the equity method when an associate's equity changes outside comprehensive income

The Interpretations Committee received a request to:

a. correct an inconsistency between the requirements of paragraphs 2 and 11 of IAS 28 and IAS 1 *Presentation of Financial Statements* (revised 2007) regarding the description and application of the equity method. This inconsistency arose when IAS 1 made a consequential amendment to paragraph 11 of IAS 28 as part of the 2007 revision to IAS 1; and
b. clarify the accounting for the investor's share of the other changes in the investee's net assets that are not the investor's share of the investee's profit or loss or other comprehensive income, or that are not distributions received; for example, how to recognise the changes in net assets of an associate that result from the associate entering into a transaction with its subsidiary's non-controlling shareholders.

This issue has been discussed by the Committee over several meetings since March 2011 as a result of the Board's request that the Committee should consider the issue in order to assist the Board in deciding whether and how the Board should amend IAS 28 to address that issue. The Committee has therefore been trying to develop principles that the Board could use in a future amendment.

At this meeting, the Committee reaffirmed the following tentative decisions from previous meetings:

- where an investor's share ownership interest in the associate is reduced, whether directly or indirectly, the impact of the change should be recognised in profit and loss of the investor; and
- where an investor's share ownership interest in the associate increases, whether directly or indirectly, the impact of the change should be accounted for as an incremental purchase of the associate and should be recognised at cost.

The Committee also considered the accounting by the investor in the following situations:

- equity-settled share-based payments of the associate; and
- written call options issued by the associate for an asset such as cash or property, plant and equipment.

The Committee was concerned about the complexity that would need to be introduced into IAS 28 to reflect the accounting for these types of transactions. Consequently, the Committee instructed the staff to recommend to the Board:

- that IAS 28 should be amended to incorporate the tentative decisions from the previous meeting, but
- not to address equity-settled share-based payments or written call options in the amendment to IAS 28.

Go to the top of this page

IFRS Interpretations Committee tentative agenda decisions

The Interpretations Committee reviewed the following matters and tentatively decided that they should not be added to the Committee's agenda. These tentative decisions, including recommended reasons for not adding the items to the Committee's agenda, will be reconsidered at the Committee meeting in July 2012. Constituents who disagree with the proposed reasons, or believe that the explanations may contribute to divergent practices, are encouraged to e-mail those concerns by ***22 May 2012*** *to: ifric@ifrs.org. Communications will be placed on the public record unless the writer requests confidentiality, supported by good reason, such as commercial confidence.*

IAS 1 *Presentation of Financial Statements and IAS 12 Income Taxes*—Presentation of payments of non-income taxes

The Interpretations Committee received a request seeking clarification of whether production-based royalty payments payable to one taxation authority that are claimed as an allowance against taxable profit of another taxation authority should be presented as an operating expense or a tax expense in the statement of comprehensive income. As the basis for this request, the submitter assumed that the production-based royalty payments are, in themselves, outside the scope of IAS 12 *Income Taxes* while the tax payable to the other taxation authority is within the scope of IAS 12. The Committee used this same premise when discussing the issue.

The Committee observed that the line item of 'tax expense' that is required by paragraph 82(d) of IAS 1 *Presentation of Financial Statements* is intended to require an entity to present taxes that meet the definition of income taxes under IAS 12. The Committee also noted that it is the basis of the calculation that determines whether a tax meets the definition of an income tax. Neither the manner of settlement of a tax liability nor the factors relating to recipients of the tax is a determinant of whether an item meets that definition.

The Committee further noted that royalty payments should not be treated differently from other expenses that are outside the scope of IAS 12, all of which may reduce income tax payable. Accordingly, because the production-based royalties do not meet the definition of an income tax they should not be presented as an income tax expense in the statement of comprehensive income.

On the basis of applying the analysis above the Committee [decided] not to add this issue to its agenda.

IAS 12 *Income Taxes*—Accounting for market value uplifts introduced by a new tax regime

The Interpretations Committee received a request to clarify the accounting for market value uplifts introduced in a proposed tax regime in a jurisdiction.

In calculating taxable profit under the proposed tax regime, entities will be permitted to calculate tax depreciation for certain mining assets using the fair value of the assets as of a particular date as the 'starting base allowance', rather than the cost or carrying value of the assets. If there is insufficient profit against which the annual tax depreciation can be used, it is carried forward and is able to be used as a deduction against taxable profit in future years.

The Committee noted that the starting base allowance, including the part that is attributable to the fair value uplift, is attributed to the related assets under the tax regime and will become the basis for depreciation expense for tax purposes. Consequently, the market value uplift forms part of the related asset's 'tax base', as defined in paragraph 5 of IAS 12. The committee observed that IAS 12 requires an entity to reflect an adjustment to the tax base of an asset that is due to an increase in the deductions available as a deductible temporary difference. Accordingly, the Committee noted that a deferred tax asset should be recognised to the extent it meets the recognition criteria in paragraph 24 of IAS 12.

On the basis of applying the analysis above, the Committee [decided] not to add this issue to its agenda.

Go to the top of this page

Issues considered for *Annual Improvements*

The Interpretations Committee assists the IASB *in Annual Improvements by reviewing proposed improvements to IFRSs and making recommendations to the Board. Specifically, the Committee's involvement includes reviewing and deliberating issues for their inclusion in future exposure drafts of proposed* Improvements to IFRSs *and deliberating the comments received on the exposure drafts. When the Committee has reached consensus on an issue included in Annual Improvements, the recommendation (including finalisation of the proposed amendment or removal from Annual Improvements) will be presented to the Board for discussion, in a public meeting, before being finalised. Approved Improvements to IFRSs (including exposure drafts and final standards) are issued by the Board.*

Issues recommended for inclusion in the 2011-2013 cycle for Annual Improvements

IAS 16 *Property Plant and Equipment and IAS 38 Intangible Assets*—Revenue-based depreciation method

The Interpretations Committee received a request to clarify the meaning of the term 'consumption of the expected future economic benefits embodied in the asset' in paragraphs 97 and 98 of IAS 38 *Intangible Assets*, when determining the appropriate amortisation method for intangible assets of service concession arrangements (SCA) that are within the scope of IFRIC 12 *Service Concession Arrangements*. The Committee was asked to consider whether:

a. a revenue-based amortisation method better reflects the economic reality of the underlying contractual terms; or
b. a time-based amortisation method is most appropriate, because it reflects the duration of the SCA and the fact that the entity received a licence to operate the infrastructure; or
c. a units-of-production method of amortisation is adequate, because it reflects the physical wearing out of the underlying asset granted to the operator.

At the November 2011 meeting the Committee noted that the principle in IAS 38 is that an amortisation method should reflect the pattern of *consumption* of the expected future economic benefits of the asset and not the pattern of generation of expected future economic benefits from the use of the asset in the business. The Committee directed the staff to draft a proposed annual improvement to address this issue.

At the March 2012 meeting, the Committee discussed a proposal to amend IAS 16 *Property, Plant and Equipment* and IAS 38. The Committee decided to recommend to the Board that it should amend IAS 16 and IAS 38 to prohibit the use of a depreciation and/or amortisation method that reflects the pattern of generation of economic benefits from operating the business instead of a pattern of consumption of expected future economic benefits of the asset. This amendment is proposed for inclusion in the next Annual Improvements cycle.

Issues with recommendations not to be added to Annual Improvements

The Interpretations Committee deliberated an issue for consideration within Annual Improvements. The Committee decided not to recommend that the Board should add the following issue to Annual Improvements.

IAS 39 *Financial Instruments: Recognition and Measurement*—Term-extending options in fixed rate-debt instruments

The Interpretations Committee received a request to address an issue related to embedded derivatives and whether they would need to be separated from the host contract under IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments*).

Specifically, the submitter requested that the Committee should clarify whether the issuer of a fixed-rate debt instrument that contains an embedded term-extending option within the scope of IAS 39 (or IFRS 9), should either:

a. separate the term-extending option from the host debt instrument and account for the term-extending option as a derivative; or
b. not separate the term-extending option from the host debt instrument. Instead, the issuer would treat the term-extending option as an integral part of the continuing host debt instrument if the term-extending option is exercised.

At the January 2012 Board meeting, the IASB and FASB boards decided to jointly redeliberate selected aspects of their classification and measurement models for financial instruments to seek to reduce key differences. The requirement to bifurcate and the basis for any bifurcation of financial assets is a topic that the boards have agreed to consider jointly along with any related implications for financial liabilities (including the need for symmetry in accounting for financial assets and financial liabilities).

Consequently, the Committee decided not to address this issue at this stage because there is a related Board project currently underway. The Committee asked the staff to make the Board aware of this issue so that the Board can consider this issue if this issue should fall within the scope of the boards' redeliberations.

The Committee decided that if the Board does not address this issue as part of its redeliberations, then the Committee will revisit this issue and consider whether guidance should be provided to clarify the accounting for the issuer of a fixed-rate-debt instrument that includes a term-extending option.

Go to the top of this page

IFRS Interpretations Committee work in progress

IFRS 11 *Joint Arrangements*—acquisition of interest in a joint operation

The Interpretations Committee received a request to clarify the application of IFRS 3 *Business Combinations* by:

- joint operators for the acquisition of interests in joint operations as defined in IFRS 11; and
- venturers for the acquisition of interests in jointly controlled operations or assets as specified in IAS 31 *Interests in Joint Ventures*.

in circumstances where the activity of the joint operation or the activity of the jointly controlled operations or assets constitutes a business, as defined in IFRS 3.

At the January 2012 meeting the Committee decided to recommend to the Board that the Committee should develop guidance on behalf of the Board for the accounting for the acquisition of an interest in a joint operation in circumstances in which the activity of the joint operation constitutes a business as defined in IFRS 3.

At this meeting, the Committee agreed that such guidance should make general reference to the relevant principles of business combination accounting and related disclosure requirements in IFRS 3 and other IFRSs and include minimal application guidance. The Committee also decided to propose that issues on which the Committee noted diversity in practice should be specifically identified in the proposed amendment, ie:

- measuring identifiable assets and liabilities at fair value with few exceptions;
- recognising acquisition-related costs as expenses in the periods in which the costs are incurred and the services are received, with the exception that the costs to issue debt or equity securities are recognised in accordance with IAS 32 *Financial Instruments: Presentation* and IFRS 9 *Financial Instruments*;
- recognising deferred tax assets and deferred tax liabilities arising from the initial recognition of assets and liabilities except for deferred tax liabilities arising from the initial recognition of

goodwill; and

- recognising the residual as goodwill.

The Committee also discussed whether the proposed guidance should be applied by the joint operator on the *formation* of a joint operation. However, the Committee did not reach a consensus on this issue and decided that the recommendation to the Board would not address this because it was not the question that was submitted to the Committee.

The staff will present the Committee's recommendation at a future Board meeting and at that meeting the staff will ask the Board whether the Board agrees with the Committee's proposed amendment which provides guidance for the acquisition of an interest in a joint operation in circumstances in which the activity of the joint operation constitutes a business as defined in IFRS 3.

IAS 7 *Statement of Cash Flows*—Review of requests in relation to IAS 7

The IASB asked the Interpretations Committee to review requests that it had received in relation to IAS 7 with a view to determining whether it could look collectively at issues that the Committee had recently discussed regarding the classification of cash flows under IAS 7. The requests reviewed were:

a. cash payments for deferred and contingent consideration arising from a business combination within the scope of IFRS 3 *Business Combinations* (November 2011);
b. cash flows for an operator in a service concession arrangement within the scope of IFRIC 12 *Service Concession Arrangements* (November 2011);
c. cash flow statement—classification of value added tax (Agenda decision, November 2004);
d. classification of expenditure on unrecognised assets (Annual Improvements, April 2009);
e. guidance on cash equivalents as defined by IAS 7 (Agenda decision, May and July 2009);
f. classification of interest paid that is capitalised (Annual Improvements, 2010-2012 cycle);
g. classification in the statement of cash flows of the flows arising from the settlement of contingent consideration in a business combination (Agenda decision, January 2012); and
h. classification of cash flows relating to construction services under service concession arrangements (Annual Improvements, 2011-2013 cycle).

The Committee noted that two 'principles of classification' in IAS 7 have been used to support the Committee's decisions (either for issuing an agenda decision or for proposing an annual improvement):

a. cash flows in IAS 7 should be classified in accordance with the nature of the activity to which they relate, following the definitions of *operating, investing* and *financing* activities in paragraph 6 of IAS 7; and
b. cash flows in IAS 7 should be classified consistently with the classification of the related or underlying item in the statement of financial position. This approach could also lead, in some circumstances to splitting transactions into their different *operating, investing* and *financing* components.

The Committee observed that the primary principle behind the classification of cash flows in IAS 7 is that cash flows should be classified in accordance with the nature of the activity in a manner that is most appropriate to the business of the entity in accordance with the definitions of *operating, investing* and *financing* activities in paragraph 6 of IAS 7. The Committee noted that it will use this as a guiding principle when analysing future requests on the classification of cash flows. The Committee also recommended that the Board should clarify the primary principle behind the classification of cash flows in IAS 7.

At a future meeting the staff will present to the Committee an analysis that will consider some other fact patterns that would illustrate the application of the identified principle behind the classification of the cash flows. The staff will report the Committee's observations to the Board at a future meeting.

SIC-13 *Jointly Controlled Entities—Non-Monetary Contributions by Venturers* and IAS 28 *Investments in Associates and Joint Ventures* (revised in 2011) —Definition of the term 'non monetary asset' in SIC 13 and IAS 28 (revised in 2011)

The Interpretations Committee received a request to clarify whether a business meets the definition of a 'non-monetary asset'. The question was asked in the context of identifying whether the requirements of

SIC-13 *Jointly Controlled Entities— Non-Monetary Contributions by Venturers* and IAS 28 *Investments in Associates and Joint Ventures* (revised in 2011) apply where a business is contributed to:

- a jointly controlled entity (JCE) as defined in IAS 31 Interests in Joint Ventures; or to:
- a joint venture (JV) as defined in IFRS 11 Joint Arrangements; or to:
- an associate

in exchange for an equity interest in that JCE/JV or associate.

At the January 2012 meeting, the Committee noted that this matter is related to the issues arising from the acknowledged inconsistency between the requirements in IAS 27 *Consolidated and Separate Financial Statements* and SIC-13, in dealing with the loss of control of a subsidiary that is contributed to a JCE/JV or an associate. The Committee directed the staff to perform further preliminary analysis of what might be the ways in which the Board could address this matter.

At the March 2012 meeting, the Committee discussed various alternatives that would address the inconsistency noted. With regard to a business that is contributed to a JCE/JV or associate, the Committee expressed support for a full gain recognition on the loss of control of the business (whether the business is housed in a legal entity or not).

The Committee decided to ask the Board whether it wants the Committee to consider further how to resolve the inconsistency between the requirements in IAS 27 and those in SIC-13 on the basis of the different alternatives discussed.

The Committee also decided to inform the Board that the Committee had not considered the related issue of contributions to joint operations as defined in IFRS 11 and the Committee was therefore not making any recommendations on that issue.

IAS 16 *Property Plant and Equipment*, IAS 38 *Intangible Assets* and IAS 17 *Leases*—Purchase of right to use land

The Interpretations Committee received a request to clarify whether the purchase of a right to use land ('land right') should be accounted for as:

- a purchase of property, plant and equipment;
- as a purchase of an intangible asset; or
- as a lease of land.

In the fact pattern submitted, the laws and regulations in the jurisdiction do not permit entities to own freehold title to land. Instead entities can purchase the right to exploit or build on land. According to the submitter, there is diversity in practice on how to account for a land right in the jurisdiction concerned.

The Committee asked the staff to bring back a proposal to the next meeting for finalising the issue with the tentative view that a proposal will be made not to add the issue to annual improvements.

Committee outstanding issues update

The Committee received a report on two new issues for consideration at a future meeting and on six outstanding issues for consideration at a future meeting. With the exception of those issues, all requests received and considered by the staff were discussed at this meeting.

IFRS Interpretations Committee’s activity in 2011

The Committee received an overview of the IFRS Interpretations Committee’s activity from January 2008 to December 2011. This was provided to the Committee for information purposes only. No decisions were made in this regard.

Go to the top of this page

Trustees review of efficiency and effectiveness of the Committee

Revisions to agenda criteria

The Committee discussed the staff proposals to revise the agenda criteria as a result of the Trustees' efficiency and effectiveness review. The Committee agreed within the proposed criteria in the context of using a broader range of tools with which to address the issues submitted to it. The proposed agenda criteria will be discussed by the Board at the March 2012 Board meeting and the views of the Committee and the Board will be reported to the Trustees in April 2012.

Role and due process of Committee's agenda rejection notices

The Committee noted the Board's tentative decisions on how the Committee should explain its reasons for not taking an issue onto its agenda (also known as agenda rejection notices). The Committee agreed with the Board's proposals. Details of the Board's tentative decisions can be found in the **February 2012 IASB Update**.

Go to the top of this page