# AGENDA PAPER

IFRS Foundation Trustees' meeting—Due Process Oversight Committee

| Brussels | 10 October 2012 | Agenda paper 3B |
|---|---|---|

**To:** David Sidwell, Chairman—Due Process Oversight Committee

**From:** Sue Lloyd

**Date:** 1 October 2012

**Re:** Update on technical activities

## Overview

This report covers updates on the following technical activities:

- Work plan projects and due process considerations
- Agenda consultation
- Post-implementation reviews
- XBRL activities

Since the last report to the DPOC in July, the IASB has:

- published amendments to clarify the transition guidance in IFRS 10 *Consolidated Financial Statements*. The amendments also provide additional transition relief in IFRS 10, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities;*
- posted to its website a draft of the forthcoming Hedge Accounting requirements that will be added to IFRS 9 *Financial Instruments*; and
- begun its Post-Implementation Review of IFRS 8 *Operating Segments* by publishing for comment a Request for Information (RFI) on the effect of implementing the Standard.

## Current projects

A list of Board papers submitted to the DPOC on due process issues since the July 2012 meeting is attached in the appendix to this paper. We have not received any new reports on due process issues. As agreed in July, in the future we will post any reports received on the website as they are submitted.

Agenda Paper 2 for the public Trustee Meeting is the report by Hans Hoogervorst. That paper provides a more general update of the IASB projects. Below is a high level summary of the status of the projects currently under way with a focus on due process considerations.

### Financial crisis related projects

#### *Financial Instruments*

Classification and Measurement: limited amendments

In July the boards concluded their joint deliberations on this project, subject to any issues that arise during drafting.

In July, the IASB also tentatively decided that once IFRS 9 *Financial Instruments* is finalised, entities that newly apply it should be required to apply **all** phases of IFRS 9 (ie the revised Classification and Measurement requirements, Impairment and Hedge Accounting) at the same time. This decision was made to improve comparability for users of financial statements.[1] This would have meant that an entity would need to be in a position to implement all phases before any of the new requirements in IFRS 9 could be applied.

In the light of these decisions, the IASB received further requests from stakeholders to make available separately as soon as possible the revised treatment of ‘own credit’ for financial liabilities. These amendments (the ‘own credit’ requirements) improve the usefulness of financial statements by removing volatility in profit or loss caused by changes in the fair value of an entity’s liabilities attributable to changes in their own credit risk. Those changes would instead be recorded in other comprehensive income (OCI).

In September 2012 the IASB responded to stakeholders’ concerns by tentatively deciding that once IFRS 9 is finalised, an entity can elect to apply the ‘own credit’ requirements for financial liabilities before the rest of IFRS 9.

In September 2012 the IASB also determined that it had complied with all the required steps in the IASB’s *Due Process Handbook*, and that it has performed enough optional due process

[1] However, those entities that-before the publication of the complete version of IFRS 9-already early applied a previous version of IFRS 9 would be able to continue applying that version and not be required to apply the final requirements until the mandatory effective date.

steps in developing the proposed limited amendments to IFRS 9 to proceed to an Exposure Draft. The IASB also agreed that, given the limited scope of the proposed amendments to IFRS 9, additional time in excess of the normal 120-day period set out in the *Due Process Handbook* is not needed. The due process analysis has been provided to the DPOC separately[2].

The IASB expects to issue an Exposure Draft in the fourth quarter of 2012. The Exposure Draft will include the proposal regarding the acceleration of the 'own credit' requirements outlined above. The FASB will also issue an exposure draft on classification and measurement of financial instruments around the same time. The exposure drafts will reflect joint decisions made by the boards, although given the different stage of development of our projects (the IASB is revising IFRS 9 whereas the FASB is proposing completely new guidance), the documents will not be identical.

Impairment

The IASB has twice exposed impairment proposals for comment, and since July 2011 has been developing with the FASB an expected loss model that is substantially different from the proposals previously exposed. That model would require expected losses to be recognised on all financial assets subject to impairment accounting. However, only a portion of the expected losses would be recognised initially, with full lifetime losses being recognised only when an asset has deteriorated by a meaningful amount.

In July 2012, after discussing the tentative impairment decisions with US stakeholders, the FASB decided to explore a different approach–one still based on expected losses–but where lifetime expected losses are recognised for all loans from initial recognition. Since July the FASB has addressed detailed aspects of this approach and will share its findings at an education session with the IASB.

The IASB staff have undertaken extensive outreach on the model that was developed with the FASB and will provide feedback on the model to the IASB in October 2012.

The IASB continues to have an open line of communication with the FASB and will continue to discuss developments. However, the IASB does not support the recognition of lifetime expected losses when a financial asset is first recognised as it does not believe that appropriately reflects the economic situation.

The timing of the forthcoming Exposure Draft on Impairment will depend on any modifications that the IASB decides are necessary on the basis of the latest outreach, but at this time we are still aiming to publish an Exposure Draft in the fourth quarter of 2012. The

[2] See AP 6D *Financial Instruments: Classification and Measurement - Due process considerations for proposing limited amendments to IFRS 9* and AP 6E *Financial Instruments: Classification and Measurement - Exposure Draft comment period and permission to begin the balloting process* from the September 2012 IASB meeting.

IASB is aware of the importance of publishing an Exposure Draft as soon as possible but needs to balance that with ensuring that the document is of the best possible quality before it is published.

Hedge Accounting

*General Hedge Accounting*

In September 2012 the IASB posted to its website a draft of the forthcoming general hedge accounting requirements that will be added to IFRS 9. As previously discussed, the IASB is not seeking comments on the draft. It is being made available for information purposes to enable constituents to familiarise themselves with the document and will provide the IASB with the opportunity to undertake an extended fatal flaw process. The draft will remain on the website until early December 2012, after which the IASB intends to incorporate the Hedge Accounting requirements into IFRS 9 subject to confirming compliance with all due process steps.

*Accounting for macro hedges*

The IASB continues to discuss the “11 steps” that it started discussing in November 2011. It is aiming to publish a Discussion Paper in 2013.

## Memorandum of Understanding projects

***Leases***

The IASB’s discussions on the Leases project are now substantially complete. During redeliberations on the Leases project, the boards decided to significantly revise the proposals that were included in the original *Leases* Exposure Draft (issued 2010). The main areas of change include the lessee accounting model—specifically, how the lessee recognises lease expense in its statement of comprehensive income for some leases; the lessor accounting model; the accounting for variable lease payments and renewal options; and the definition of a lease. The revisions to the proposals were made in response to feedback on the Exposure Draft received from stakeholders as a result of substantial issues that emerged during the comment period. For example, many stakeholders had significant concerns that the original proposed lease accounting model did not accurately portray the economics of all lease transactions.

The revised decisions result in fundamental changes to the original proposals for both lessee and lessor accounting. Consequently, in accordance with the *IASB Due Process Handbook*,[3]

[3] Paragraph 47 : *In considering the need for re-exposure, the IASB*

- *identifies substantial issues that emerged during the comment period on the exposure draft that it had not previously considered*
- *assesses the evidence that it has considered*

the IASB wishes to seek stakeholders' views on these changes and also wishes to provide interested parties with the opportunity to comment on the revisions. Consequently, as previously noted, in July 2011 the boards agreed unanimously to re-expose the revised proposals for a common Leases Standard. The due process analysis will be provided to the DPOC separately.

The publication timetable is affected by several FASB-only issues that remain outstanding, primarily related to private companies. The boards aim to issue exposure drafts in the first quarter of 2013. During the comment period, the boards plan to conduct additional outreach with users of financial statements and with entities that undertake lease activities. Depending on the nature and extent of the issues raised, the boards expect a final Standard to be published in the second half of 2013.

#### *Revenue Recognition*

As discussed in the July meeting, the comment period on the re-exposure draft ended in March 2012. Redeliberations on the Revenue Recognition are currently on-going. The objective is to complete the substantive deliberations in late 2012. However, the boards will need to be disciplined to keep to this timetable. During the redeliberations, targeted outreach is still continuing. Subject to completion of due process steps, it is anticipated that a final Standard would be issued in mid-2013.

### Other technical projects

#### *Insurance Contracts*

*Insurance Working Group*

The Insurance Working Group met on 25 and 26 June 2012. The IASB staff reported the status of the Insurance Contracts project decisions to the working group and received input on the few remaining decisions for the project. The IASB staff also discussed the working groups' questions about convergence and the need to balance convergence, quality and timeliness. The IASB staff noted that while they are not in identical places, the IASB and the FASB have worked to minimise their differences[4]**.**

---

- *evaluates whether it has sufficiently understood the issues and actively sought the views of constituents*
- *considers whether the various viewpoints were aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions on the exposure draft.*

[4] Currently the differences are as follows:

- whether the risk adjustment should be explicitly included in measurement of the liability and remeasured each period (IASB) versus implicitly included in measurement and run off over contract life (FASB);

The IASB staff will put working drafts on the IASB website that implement key decisions in the project and invite the working group to provide comments on the drafting.

*Re-exposure versus review draft*

The redeliberations on the Insurance Contracts project are not yet complete. However, it was determined that enough decisions had been made to enable the IASB to assess whether re-exposure is required. The IASB also decided that it would be helpful to constituents to discuss re-exposure as soon as possible. The staff noted that if the IASB decided that re-exposure was not required, it still would have been necessary to reconfirm whether that conclusion was appropriate on completion of the redeliberations.

Consequently, in September 2012 the IASB discussed whether to re-expose the proposals or to move forward with a Review Draft of the Insurance Contracts model, accompanied by targeted outreach. The IASB noted that there have been significant changes to some of the proposals that were included in the original *Insurance Contracts* Exposure Draft (July 2010). These changes relate to the measurement of the insurance contracts that require payments linked to the performance of underlying items (ie participating contracts); the decision to present premiums, claims and expenses in the statement of comprehensive income; the offsetting of changes in estimate of cash flows in the residual margin (ie unlocking of the residual margin); the use of other comprehensive income to present changes in the liability arising from changes in the discount rate; and the transition proposals.

However, the core principles in the Exposure Draft have largely remained intact and the changes have mostly clarified or simplified the application of those principles. In some cases the changes even result in accounting that is more consistent with existing requirements and practices. During redeliberations, the IASB has also made extensive efforts to consult interested parties and to assess whether there are unintended consequences as a result of the changes made. The IASB staff has made available on its public website reports of the IASB's tentative decisions and extracts of a working draft implementing some decisions and has specifically invited comment on unintended consequences.

---

- how changes in the residual margin (unlocking) should be recognised (IASB: offset against residual margin, FASB: recognise in profit or loss);
- eligibility for short-duration contract treatment (IASB: premium allocation approach is permitted when measurement is similar to building block approach, FASB: premium allocation approach is required when specific criteria are met);
- measurement of the liability for incurred claims for short-duration contracts (IASB: measure at risk—adjusted present value of cash flows, FASB: measure at present value of cash flows only);
- the definition of acquisition costs (IASB: residual margin shows expected profit after deducting costs of acquiring and fulfilling liability, FASB: same as IASB but excluding the portion deemed to not result in the issuance of contracts) ; and
- whether investment contracts with discretionary participation features should be in the scope of the insurance contracts standard (IASB: include, FASB: exclude).

The IASB understands that some of the changes respond directly to stakeholders' requests and would not automatically result in, or require, re-exposure in accordance with the terms of the *Due Process Handbook*. However, operational challenges may arise as a result of the magnitude of these changes. Input on the relative cost and benefit of the proposals, either through field work or through re-exposure, would also be valuable for the IASB. Consequently, the IASB decided that on balance it should re-expose the Insurance Contracts proposals.

Furthermore, notwithstanding the decision to re-expose, the IASB also recognises the need to finalise the Insurance Contracts project expeditiously, because currently IFRS does not provide guidance on accounting for insurance contracts. Consequently, the IASB has decided that while the Exposure Draft will set out the whole draft IFRS, the questions in the re-exposure draft will be targeted, instead of requesting responses on all issues including those unchanged from the original Exposure Draft.

The due process analysis has been provided to the DPOC separately.[5]

*Next steps*

The boards are continuing their deliberations. The IASB estimates that it will conclude the major technical discussions on the project in the second half of 2012 and aims to publish the new Exposure Draft in the first half of 2013.

***Investment Entities***

The IASB has completed its planned deliberations on this project. The decisions introduce an exception that will require Investment Entities to measure their subsidiaries at fair value through profit or loss rather than consolidating them. In conjunction with these decisions, in July 2012 the IASB considered whether re-exposure was necessary. At the July 2012 meeting all IASB members agreed that:

- the decisions made during redeliberations did not change the basic concepts in the *Investment Entities* Exposure Draft but instead resulted in a number of refinements to the proposals that were in response to comments received;
- the proposed changes affect only a limited number of entities; and
- the issues involved are well understood by both the IASB and its constituents and therefore no new information would be expected to arise from re-exposure.

Consequently, the IASB unanimously agreed that none of the amendments require re-exposure. The due process analysis was provided to the DPOC separately.[6]

[5] See AP16D *Insurance Contracts – Review draft or re-exposure* and *AP16E Insurance Contracts – Due process summary for the insurance contracts project* from the September 2012 IASB Board meeting.
[6] See AP8G *Investment Entities Due Process Considerations* from the July 2012 IASB Board meeting

The IASB plans to issue the final Investment Entity requirements in the fourth quarter of 2012. The effective date will be 1 January 2014 with early application permitted.

The Investment Entity deliberations were mainly carried out jointly with the FASB. However, the FASB is addressing the accounting for investment entities more broadly than the IASB, whose focus was solely on an exemption from consolidation. Consequently, the boards' final requirements will be similar but not identical.

## *Narrow-scope projects*

### *Other projects*

As a result of submissions to the Interpretations Committee (which proposed amendments to the IASB because of diversity in practice today), the IASB tentatively decided to make the following amendments to IFRSs:

- September 2012: to add guidance to IAS 28 *Investments in Associates and Joint Ventures* and IFRS 10 on the accounting for sales of assets between an investor and its associate or joint venture, and to specify whether the gain on such transactions should be recognised in full or in part.

- September 2012: to add additional guidance to IFRS 11 on the accounting for an interest in a joint operation when that joint operation includes a business. There is concern that the current diversity in practice under IAS 31 *Interests in Joint Ventures* will continue when IFRS 11 comes into effect in 2013.

- July 2012: to provide additional guidance in IAS 28 on how an investor should account for its share of the changes in the net assets of an associate (or joint venture) that are not recognised in profit or loss or other comprehensive income of the associate (so-called 'other net asset changes').

The IASB aims to publish the above amendments in three separate Exposure Drafts in the fourth quarter of 2012. All documents will have the standard 120 day comment period.

### *IAS 8—Effective date and transition methods*

In the July meeting we noted issues that were raised relating to the disclosures required in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* when there is a change in accounting policy. In September 2012 the IASB addressed the more urgent issues that were raised at a Standard level in its IFRS 9 deliberations.

As a result, the IASB staff plan to propose in the October 2012 IASB meeting that the IASB should suspend work on an exposure draft proposing clarifications or changes to IAS 8 and instead address the remaining broader IAS 8 issues as part of the Disclosure Chapter work in the Conceptual Framework project.

***Annual Improvements 2010-2012***

The 2010–2012 Annual Improvements Exposure Draft was published in May 2012. The comment period ended on 5 September 2012. 83 comment letters have been received and are being reviewed. A summary of the comment letters received is due to be presented to the Interpretations Committee in November 2012. After the Interpretations Committee has discussed the comments received on each issue, its recommendations on whether and how to finalise each proposed amendment will be presented to the IASB for finalisation.

***Annual Improvements 2011-2013***

The IASB has discussed five issues for inclusion in the Exposure Draft for the 2011–2013 cycle of Annual Improvements. The IASB expects to publish the 2011-2013 Exposure Draft in November 2012.

## Draft Interpretations

***Levies***

In May 2012 the Interpretations Committee published a draft Interpretation proposing clarifications to when a liability to pay certain levies should be recognised. The comment period ended on 5 September 2012. 53 comment letters have been received and are being reviewed. A summary of the comment letters is due to be presented to the Interpretations Committee in November 2012.

***NCI Puts***

In May 2012 the Interpretations Committee also published a draft Interpretation proposing clarifications to the accounting for puts over non-controlling interests. The comment period will end on 1 October 2012.

## Educational material: IFRS 13 *Fair Value Measurement*

The IASB staff, with the assistance of a valuation working group, are preparing educational material to support IFRS 13 *Fair Value Measurement*. This will be published in chapters as they are developed. This is to ensure that the additional guidance will be available on a timely basis.

It is planned that the first chapter of the educational material related to IFRS 13 will be published later this year (2012). That chapter will address the fair value measurement of unquoted equities.

It has been reviewed by four IASB members, which complies with the procedures in the *Due Process Handbook* that is currently out for comment. In addition, before it is finalised, the draft chapter will be posted on the IASB website for a period of about six weeks. The IASB is not seeking comments on the draft. It is being made available for information purposes to enable constituents to familiarise themselves with the document and will provide the IASB with the opportunity to undertake an extended fatal flaw process.

The IASB staff will begin drafting the second chapter (on applying the 'highest and best use' concept) once the first chapter is posted.

## Agenda Consultation

As previously discussed, in July 2011 the IASB launched its first formal public agenda consultation on its future work plan to seek input from all interested parties on our strategic direction and on the broad overall balance of the work plan. In response to the agenda consultation, the IASB agreed to give priority to certain projects, including work on the *Conceptual Framework*, Rate-regulated Activities, and amendments to IAS 41 *Agriculture*.

In September 2012 the IASB began discussion of these projects, and agreed to add a limited-scope project on IAS 41 for bearer biological assets (BBAs) to its technical agenda. The IASB decided that it is unlikely that a limited-scope project for BBAs would need a Discussion Paper because of the research already undertaken by a national standard-setter. Consequently, the IASB aims to publish an Exposure Draft in the first half of 2013.

The IASB also discussed the approach to the *Conceptual Framework* project, and agreed that it should focus on elements of financial statements, measurement, reporting entities, presentation and disclosure. The IASB agreed that the work should be towards a single Discussion Paper, rather than separate Discussion Papers for each area.

Finally, the IASB discussed a Standards-level project for Rate-regulated Activities. The IASB had previously undertaken a Rate-regulated Activities project in 2008–2010 and agreed that, on the basis of the divergent views and feedback received from the previous project, a Discussion Paper should first be published in advance of developing an IFRS or amending an existing IFRS. The IASB aims to issue a Discussion Paper in the fourth quarter of 2013. The IASB also considered publication of an interim Standard in response to stakeholders' requests for interim guidance until a more comprehensive solution is developed. This is especially relevant for jurisdictions that have significant rate-regulated activities and have already adopted IFRS, but where lack of guidance is creating diversity in practice.

The proposals for IAS 41 and Rate-regulated Activities will be discussed at the Advisory Council meeting in October 2012. The *Conceptual Framework* items are part of an existing project that has been previously discussed with the Advisory Council.

The IASB aims to publish a Feedback Statement in the fourth quarter of 2012 explaining how the IASB has responded to the agenda consultation.

## Post-implementation reviews (PIR)

On 26 June 2012 the IASB began the public part of its review of IFRS 8 *Operating Segments* by publishing for comment a Request for Information (RFI) on the effect of implementing the Standard. The RFI has a 120-day comment period. During the comment period, the staff are co-ordinating outreach and evidence-gathering events with various stakeholder groups, including investor groups, national accounting standard-setters and other regional bodies and securities regulators. The next discussions of the PIR of IFRS 8 will be in early 2013, when the topic will be the analysis of comment letters received in response to the RFI.

The IASB expects to apply the experience gained from its first PIR to inform its planning for the PIR of IFRS 3 *Business Combinations* later in 2013.

## XBRL activities

*Potential due process review*

The XBRL team has been considering potential changes to its due process to align the public consultation of taxonomy interim releases to issue dates of IFRSs. This topic will be discussed with the XBRL Advisory Committee (XAC) and the XBRL Quality Review Team (XQRT) in October 2012. Once we have their feedback, we will consider whether it would be helpful to have a public *Request for Information* to solicit feedback on the XBRL processes in general.

*Releases for new/amended IFRSs*

In line with the timing of the related staff publications, an interim taxonomy for Investment Entities will be released for XQRT to review early in November 2012 with a further interim taxonomy update publication planned for Hedge Accounting in December 2012.

**Appendix to AP3B**

## List of papers submitted to the DPOC since the July 2012 meeting

| **Subject** |
|---|
| **Classification and Measurement: Limited amendments—**September 2012 Board papers<br>• AP 6D *Financial Instruments: Classification and Measurement - Due process considerations for proposing limited amendments to IFRS 9*<br>• AP 6E *Financial Instruments: Classification and Measurement—Exposure Draft comment period and permission to begin the balloting process* |
| **Insurance—**September 2012 Board papers<br>• AP16D *Insurance Contracts—Review draft or re-exposure*<br>• AP16E *Insurance Contracts—Due process summary for the insurance contracts project* |
| **Leases**—July 2012 Board papers<br>• AP 3H *Due process*<br>• AP 3G *Exposure Draft comment period and permission to begin the balloting process* |