

ADMIN PAPER

IFRS Foundation Trustee Meeting – Due Process Oversight Committee

Frankfurt

15-17 October 2013

Agenda paper 3B

Memorandum

To: Scott Evans, Chairman – Due Process Oversight Committee

From: Sue Lloyd/Alan Teixeira

Date: 4 October 2013

Re: Technical Projects - update

Overview

1. Since the last meeting in July we have published the exposure drafts on the accounting for Bearer Plants and on proposed amendments to the IFRS for SMEs. The Conceptual Framework Discussion Paper was also published.
2. The IASB has also published its Feedback Statement on the post implementation review (PIR) of IFRS 8 *Operating Segments* and launched its post implementation review of IFRS 3 *Business Combinations*.
3. We are continuing to progress the four major projects: Financial Instruments, Revenue Recognition, Leases and Insurance Contracts. The new hedge accounting requirements are expected to be published shortly. We had hoped to publish the new Revenue Recognition requirements shortly too but are now addressing some final matters prior to publication.
4. The Interpretations Committee has also continued to be very active.
5. A copy of the work plan as at 23 September 2013 is attached as Agenda Paper (AP) 3B(i).

Due Process

6. As previously requested by the DPOC, a list of papers that were posted less than 5 working days before an IASB meeting is attached in Appendix A to this paper.
7. Below is a summary of the status of the projects currently underway with a focus on due process considerations.

Financial Instruments

8. In July 2013 the IASB tentatively decided to defer the mandatory effective date of IFRS 9 *Financial Instruments* from 1 January 2015. The new mandatory effective date will be decided at a later date. The appropriate date will depend both on when deliberations are completed and also on the final details of the expected credit loss model which is critical to determining the appropriate implementation period. This change to IFRS 9 is expected to be published shortly¹.

IFRS 9—Classification and Measurement (limited amendments)

9. As discussed in previous meetings, in November 2012 the IASB published an Exposure Draft *Classification and Measurement: Limited Amendments to IFRS 9 (Proposed amendments to IFRS 9 (2010))*. This Exposure Draft proposed limited amendments to the classification and measurement requirements for financial instruments already contained in IFRS 9. The main changes proposed in the ED were to clarify the notion of principal and interest, to propose the introduction of a fair value through OCI category for simple debt investments and to propose clarifications to the concept of ‘holding to collect’ contractual cash flows.
10. The FASB issued an Exposure Draft on the classification and measurement of financial instruments in February 2013. While the Exposure Drafts reflect joint decisions made by the boards, 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 were not identical.
11. A summary of the comments received on each of these documents has been presented to the boards. At the September meeting joint redeliberations commenced with discussion of the features of debt instruments with simple features (‘solely principal and interest’) that would be eligible for measurement other than at fair value through profit or loss. The next topic that will be deliberated will be the business model.
12. The IASB tentatively decided to amend IFRS 9 so that entities can apply the ‘own credit’ requirements in IFRS 9 before other parts of the standard. This means that entities would

¹ This change along with the change related to ‘own credit’ will be published with the new hedge accounting requirements as all of these changes relate to IFRS 9.

be permitted to choose to present the changes in fair value for liabilities measured at fair value under the fair value option in Other Comprehensive Income before making any other changes to their accounting for financial instruments in accordance with IFRS 9.

13. The objective is to complete the substantive redeliberations on classification and measurement by the end of 2013.

Impairment

14. The objective of the Impairment project is to increase the usefulness of financial statements by improving the transparency of information about the credit quality of loans subject to impairment², and improving the timeliness of recognition of expected credit losses.
15. In March 2013 the IASB published an Exposure Draft *Financial Instruments: Expected Credit Losses*. The proposals in that document were based on the model that the IASB had been developing jointly with the FASB. The proposals would result in expected credit losses always being recognised (from when a financial instrument is first purchased or originated) with full lifetime expected credit losses being recognised when a financial instrument suffers a significant deterioration in credit quality.
16. As discussed at previous meetings, in July 2012 the FASB decided to explore a different approach—one still based on expected credit losses, but in which full (all) lifetime expected credit losses are recognised for all loans from initial recognition.
17. In late December 2012, the FASB published their Exposure Draft on impairment. The IASB and FASB have shared the feedback they have received on their respective exposure drafts. While many (including the Financial Stability Board) still request a converged solution, geographical differences in feedback continue to be apparent including from users of financial statements and few suggestions have been made for how convergence could be achieved. Each board is now considering changes they would make to their proposals considering the comments that they have received. Following those amendments the boards will be able to consider the prospects for further aligning the models.
18. Overall the feedback received by the IASB was supportive. In particular, there was support for a model that measures expected credit losses differently on the basis of a significant increase in credit risk and the operability of the proposals was confirmed. Some did however raise concerns about the timeliness of identification of significant increases in credit risk so the IASB will consider ways to make the model more responsive to changes in credit risk. The Accounting Standards Advisory Forum (ASAF) had the opportunity to comment on these changes at their September meeting.

²

We refer to all financial assets subject to impairment as “loans” in the Impairment section of this paper for ease of discussion.

19. The IASB aims to complete the substantive deliberations on the impairment requirements in 2013.

Hedge Accounting

20. The objective of this project is to improve hedge accounting by more closely aligning it with a company's risk management activities, thereby improving financial reporting. As previously discussed, the Hedge Accounting phase of the Financial Instruments project is not a joint project. However, the FASB sought comments from its stakeholders on the IASB's Hedge Accounting Exposure Draft.
21. At the April 2013 IASB meeting, the IASB finalised its deliberations on hedge accounting and granted the staff permission to draft the final hedge accounting requirements for inclusion in IFRS 9. These final requirements are now being balloted in preparation for publication.

Accounting for Macro Hedging

22. All planned technical discussions on the model for accounting for macro hedging, prior to publication of the Discussion Paper, have been completed. At the October board meeting the staff will ask the IASB for permission to ballot the Discussion Paper and to confirm the comment period. Publication of the Discussion Paper is planned to occur in 2013.
23. This project was discussed by the ASAF at their September meeting.

Leases

24. The objective of the Leases project is to improve the quality and comparability of financial reporting by providing greater transparency about leverage, the assets an entity uses in its operations and the risks to which it is exposed from entering into lease transactions.
25. This is a joint project with the FASB. In May 2013, the boards published a joint and revised Exposure Draft on leases, which was open for comment until 13 September 2013. Under the proposals, a lessee would report assets and liabilities for all leases of more than 12 months on its balance sheet. The recognition of lease-related expenses in the lessee's income statement for most real estate leases would be different from that for most other leases to better reflect the differing economics of those leases. The Exposure Draft also proposes some changes to the accounting applied by many equipment and vehicle lessors, which would better reflect how such lessors price their leases.
26. Extensive outreach activities have been undertaken during the comment period focussing

in particular on obtaining feedback from users of the financial statements and understanding the drivers of costs for preparers. A lot of effort has gone into reaching users of financial statements – over 35 meetings have been held involving more than 220 investors and analysts from Europe, North America, Africa, Asia and Australasia³. In addition, a series of public roundtables are planned.

27. The ASAF discussed their feedback on the exposure draft at their September 2013 meeting.
28. Redeliberations will recommence in the fourth quarter of 2013.

Revenue Recognition

29. The objective of this project is to improve financial reporting by creating a common revenue recognition Standard that clarifies principles that can be applied consistently across various transactions, industries and capital markets. The project applies to all contracts with customers (except leases, financial instruments and insurance contracts).
30. This project is near completion and the draft of the final IFRS is at an advanced stage. At the September 2013 board meeting three issues that were raised in the drafting of the final document were discussed with the boards and the staff asked for direction on how the boards would like to address these issues. These extra steps and the extensive input sought on the draft of the final document reflect the importance the boards place on ensuring that the final document is clear and operational.
31. As discussed previously, due to the importance of revenue and the broad scope of the new Standard, the IASB and the FASB intend to establish a limited life transition resource group to support preparers in the transition to the new Standard. Importantly, it is not envisaged that the group provide authoritative guidance.

Insurance Contracts

32. The objective of this project is to eliminate inconsistencies and weaknesses in existing practice by replacing IFRS 4 *Insurance Contracts* and to provide a single principle-based Standard to account for all insurance contracts.
33. The IASB published its revised Exposure Draft at the end of June 2013. Due to the importance of completing this project, and in view of the extensive debate the IASB has undertaken over the years, the exposure draft seeks feedback on five key matters on which there have been significant changes to the proposals in the 2010 Exposure Draft.

³ A summary of the outreach is available on the Leases project page of the IASB website at: <http://www.ifrs.org/Current-Projects/IASB-Projects/Leases/Documents/Lessee-accounting-investor-outreach-summary-May-to-September-2013.pdf>.

The IASB hopes that targeting its revised Exposure Draft in this way will avoid further undue delay in finalising a much-needed Standard for insurance contracts accounting.

34. The comment period for the exposure draft ends on 25 October 2013. During the comment period extensive outreach is being undertaken across a broad range of jurisdictions.
35. At the September 2013 meeting the ASAF provided feedback on the five key areas on which questions are asked in the exposure draft.

The Conceptual Framework

36. The Conceptual Framework sets out the concepts that underlie the preparation and presentation of financial statements. It is not a Standard or Interpretation and does not override any specific Standard or Interpretation. However, it identifies principles for the IASB to use when it develops and revises its IFRSs.
37. The existing Conceptual Framework has enabled the IASB to develop high quality IFRSs that have improved financial reporting. However, it does not cover some important areas and some guidance needs updating. Consequently, most respondents to the 2011 agenda consultation identified the Conceptual Framework as a priority project for the IASB.
38. The Discussion Paper, published in July 2013, is the first step towards issuing a revised Conceptual Framework. It is designed to obtain initial views and comments on important issues that the IASB will consider as it develops an exposure draft of a revised Conceptual Framework. It focuses on those areas that have caused the IASB problems in practice, including:
 - definitions of assets and liabilities;
 - recognition and derecognition;
 - the distinction between equity and liabilities;
 - measurement;
 - presentation and disclosure; and
 - other comprehensive income (OCI).
39. The 180 day comment period for the Discussion Paper ends on 14 January 2014. During the comment period, outreach is being conducted to obtain feedback on the issues included in the Discussion Paper.

Rate-regulated Activities

40. The long term objective of the Rate-regulated Activities research project is to develop a

Discussion Paper to consider whether rate regulation creates assets or liabilities in addition to those already recognised in accordance with IFRS for non-rate-regulated activities. A Request for Information *Rate Regulation* was published in March 2013 to gather more information about the common features of rate regulation. A summary of the 79 responses received was discussed in July by a formal consultative group that was formed for this project. In September 2013, the IASB began deliberations on the common features identified as being most important to distinguish rate-regulated activities from general commercial activities, and that have the biggest impact on the amount, timing and certainty of cash flows and the stability of 'regulated' earnings. Future deliberations will consider these features in the context of the developments in the Conceptual Framework project.

41. In addition, in September 2013 the staff presented an initial summary of the responses received to proposals for an interim IFRS designed to assist those adopting IFRS prior to completion of the broader project. The IASB expects to begin redeliberations on the proposals in the October 2013 meeting.

Narrow-scope projects

On-going narrow-scope projects

IAS 41—Bearer Plants

42. In June 2013, in response to the 2011 Agenda Consultation, the IASB published for public comment an Exposure Draft of proposals to include bearer plants within the scope of IAS 16 *Property, Plant and Equipment*. Bearer plants are a class of biological assets that, once mature, are held by an entity solely to grow produce over their productive life. Examples include grape vines, rubber trees and oil palms.
43. Currently, IAS 41 *Agriculture* requires all biological assets that are related to agricultural activity, including bearer plants, to be measured at fair value less costs to sell. This requirement is based on the principle that biological transformation is best reflected by fair value measurement. However, once mature, bearer plants no longer undergo significant biological transformation. Furthermore, their operation is similar to that of manufacturing. Consequently, the Exposure Draft proposes that bearer plants are accounted for in accordance with IAS 16 instead of IAS 41, thus permitting the use of either a cost model or a revaluation model. The produce growing on the bearer plants would remain under the fair value model in IAS 41.

44. The Exposure Draft is open for comment until 31 October 2013.

IAS 1—Disclosure Initiative

45. In May 2013 the IASB issued the Feedback Statement: *Discussion Forum—Financial*

Reporting Disclosure (the ‘Feedback Statement’). The Feedback Statement sets out a number of short-term and medium-term projects the IASB will be asked to consider in response to the concerns raised about financial reporting disclosure. The package of these projects is referred to as the Disclosure Initiative.

46. At its September 2013 meeting, the IASB considered the first of the proposed Disclosure Initiative projects—narrow scope amendments to IAS 1 *Presentation of Financial Statements*. These amendments are intended to clarify, rather than significantly change, existing IAS 1 requirements. However, it is considered that the relatively modest proposed amendments will address some problems that have emerged in practice in areas such as the application of materiality and determining the order of the notes to the financial statements. In October 2013, the IASB is expected to discuss further proposals as part of this project, including net debt and the presentation of subtotals of IFRS recognised amounts such as EBIT and EBITDA.
47. The Exposure Draft (that will also address disclosures about Going Concerns as described below) is scheduled to be published in the first quarter of 2014.

IAS 1—Disclosure Requirements about Assessment of Going Concern

48. IAS 1 requires that when management are aware of material uncertainties about an entity’s ability to continue as a going concern, those uncertainties should be disclosed. The submitter, the International Auditing and Assurance Standards Board (IAASB), thinks that the guidance about the disclosure of these uncertainties is not clear. A similar topic had been presented to the Advisory Council in June 2012 by the chair of the UK FRC on actions that they were taking in response to the Sharman Inquiry. The Advisory Council’s advice at that time was that perhaps the Interpretations Committee or the IASB could provide guidance on these disclosures.
49. At its March 2013 meeting the IASB discussed proposals for a narrow-scope amendment to IAS 1 that would clarify when disclosures about material uncertainties connected with going concern should be disclosed and what disclosures should be given. The IASB requested that the proposals should be further developed and since then work has been continuing. The IASB is expected to discuss the revised proposals in October 2013. It is expected that these proposals will be exposed for comment in the first quarter of 2014 (along with other proposed amendments to IAS 1 relating to work on the Disclosure Initiative and sundry amendments with respect to, for example, classification of liabilities).

IAS 27—Separate Financial Statements (Equity Method)

50. When an entity prepares separate financial statements it has the choice of measuring investments in subsidiaries, joint ventures and associates at cost or at fair value. Corporate law in some countries requires listed entities to present separate financial

statements using the equity method of accounting to measure these investments. Consequently, entities in those countries must currently prepare two sets of financial statements.

51. Feedback received from the 2011 Agenda Consultation indicated that there was strong support from stakeholders in those countries affected, particularly from Latin America, for the IASB to address this issue.
52. As a result the IASB agreed to consider a proposal to amend IAS 27 *Separate Financial Statements* to allow the use of the equity method of accounting. We aim to publish an Exposure Draft in the fourth quarter of 2013.

IAS 19—Actuarial Assumptions: Discount Rate

53. The Interpretations Committee was asked to clarify whether corporate bonds with a rating lower than ‘AA’ can be considered to be high-quality corporate (HQC) bonds for the purposes of calculating the defined benefit obligation for post-employment benefits. According to prevailing past practice, listed corporate bonds have usually been considered to be HQC bonds if they receive one of the highest two ratings given by a recognised rating agency (‘AAA’ and ‘AA’). Because of the financial crisis the number of these bonds has decreased. The Interpretations Committee discussed various proposals to address this issue but concluded that this topic is too broad for a narrow-scope amendment to IAS 19 *Employee Benefits*. It therefore asked the staff to focus on an analysis of whether ‘high quality’ is an absolute or relative concept. The Interpretations Committee discussed this analysis at its July 2013 meeting and published a tentative Agenda Decision setting out its views on the topic and its reasons for not adding the issue to its agenda. This tentative agenda decision was open for comment until 25 September 2013. The Interpretations Committee will discuss the comments received at its November 2013 meeting with a view to finalising the Agenda Decision. It will then report its conclusion to the IASB.

Put Options Written on Non-controlling Interests (NCI)

54. In March 2013, the IASB decided not to proceed with the finalisation of the draft interpretation regarding the accounting for NCI puts. The Board asked the staff to undertake further analysis on the accounting for puts over an entity’s own equity (including over NCI). Work on this issue has been continuing and the IASB is expected to discuss the new analysis of the issue in the fourth quarter of 2013. On the basis of these discussions the IASB will decide what the next steps should be.

Other new narrow-scope projects

55. A narrow-scope amendment on the unit of account for fair value measurement of equity investments in subsidiaries, associates and joint ventures is currently with the IASB for development. Since the IASB discussed this issue a question has been raised about the

application of the portfolio exception in IFRS 13 *Fair Value Measurement* to Level 1 financial instruments⁴. The IASB has decided to consider both issues before publishing any proposed amendments.

56. The IASB has also decided to propose a narrow-scope amendment to IAS 28 *Investments in Associates and Joint Ventures* to clarify the accounting for a ‘downstream’ transaction between an entity and its associate or joint venture when the gain from the transaction exceeds the carrying amount of the entity’s interest in the associate or joint venture. The exposure draft is scheduled for publication in the first quarter of 2014.

Annual Improvements

Annual Improvements 2010–2012

57. The 2010–2012 Annual Improvements Exposure Draft was published in May 2012. The Interpretations Committee has discussed the comments received on all of these annual improvements. The recommendations from the Interpretations Committee on how to finalise many of these issues were presented to the IASB in the first and second quarters of 2013. The IASB expects to issue the final requirements in the fourth quarter of 2013.

Annual Improvements 2011–2013

58. The 2011–2013 Annual Improvements Exposure Draft was published in November 2012. A summary of the comment letters received was presented to the Interpretations Committee in May 2013 and the IASB has discussed the recommendations from the Interpretations Committee on how to finalise these proposed amendments. The IASB expects to issue the final requirements in the fourth quarter of 2013.

Annual Improvements 2012–2014

59. The Interpretations Committee has so far identified four potential issues for inclusion in the Exposure Draft for the 2012–2014 cycle of Annual Improvements; one of these has been agreed by the IASB. The others will be presented to the IASB in the fourth quarter of 2013. The IASB expects to publish the 2012-2014 Exposure Draft in the fourth quarter of 2013⁵.

⁴ Level 1 financial instruments are those for which there are quoted prices in active markets for the identical financial instrument.

⁵ The publication of the various annual improvements is being coordinated to make it easier for those amending legislation and/or commenting on the new proposals.

Education Initiative

Fair value measurement – educational material

60. The Education Initiative is developing educational material to support IFRS 13 with the assistance of a valuation expert group. The material is being prepared in various chapters. A draft chapter is currently being prepared on the concept of ‘highest and best use’ in fair value measurement.

IFRS for SMEs

Comprehensive Review 2012–2014

61. As previously discussed, when the IASB issued the International Financial Reporting Standard for Small and Medium-sized Entities (*IFRS for SMEs*) in July 2009, it stated that it would undertake an initial comprehensive review of the Standard. This review would allow the IASB to assess the first two years’ experience in implementing the Standard and consider whether there is a need for any amendments. In many jurisdictions, companies started using the *IFRS for SMEs* in 2010. Consequently, the IASB commenced its initial comprehensive review in 2012.

62. In order to assist in the process of identifying which items to consider for amendment, the IASB issued a Request for Information (RfI) in June 2012 to seek public views and consulted with the SME Implementation Group, an advisory body to the IASB. After considering the feedback it received, and taking into account the fact that the *IFRS for SMEs* is still a new Standard, the IASB only proposes to make limited amendments to the *IFRS for SMEs*. The proposed amendments are not expected to result in significant changes in practice for SMEs or to have a significant impact on their financial statements.

63. The Exposure Draft of proposed amendments to the *IFRS for SMEs* was published in October 2013 with an extended comment period of 150 days to allow organisations additional time in order to solicit and consolidate the views of smaller businesses in their jurisdictions.

Guidance for micro-sized entities

64. In June 2013 the IASB staff published guidance to help micro-sized entities apply the *IFRS for SMEs*. This guidance supports the *IFRS for SMEs* and does not constitute a separate Standard for micro-sized entities.

Post-implementation review (PIR)

65. In July 2013 the IASB completed its first PIR, the review of IFRS 8. A report and

feedback statement was published by the IASB. The general conclusion of the report was that IFRS 8 is functioning as was anticipated. IFRS 8 is a converged standard so the IASB noted that in those limited areas where further investigation is warranted the IASB will liaise with the FASB and that any changes would be considered within the context of the convergence with US GAAP that was achieved with IFRS 8.

66. In July 2013 the IASB launched its PIR of IFRS 3 *Business Combinations*. IFRS 3 was undertaken in two stages, the first was completed in 2004 and the second in 2008. The review will consider both stages and will also include the changes to the presentation of consolidated financial statements that were made at the same time. Currently the PIR is in its first phase during which outreach is undertaken to identify implementation problems or unexpected costs that have arisen in the application of IFRS 3 and academic and other studies about the standard will be considered. This will be followed by a second phase when a Request for Information will be published.

Appendix A

Late IASB Board paper postings

July 2013

(Board meeting commenced 23 July 2013)

IASB Paper number	FASB Memo number	Project	Status of paper	Comment
7A-Ad.	173A-Ad.	Revenue Recognition: Collectibility	Posted 23 July	Addendum to explain Alternative C (Revenue meeting held 24 July)

September 2013

(Board meeting commenced 13 September 2013)

IASB Paper number	FASB Memo number	Project	Status of paper	Comment
6A	241	Classification & Measurement: Cover Paper	Posted 9 Sept	Late posting to finalise with FASB. Provided to IASB members on 6 Sept
6F	246	Classification & Measurement: Contractual Cash Flow Characteristics: Prepayment Features	Posted 9 Sept	Late posting to finalise with FASB. Provided to IASB members on 6 Sept
6AppA and B	App A and B to Memos 243-244	Classification & Measurement: Flowcharts to illustrate Agenda Papers	Posted 16 Sept	Flowchart to illustrate staff recommendations in Agenda Papers 6C–6D/FASB Memos 243–244 (Meeting held 18 September)