## Introduction

1. The Global Preparers Forum (GPF) met in London on 11 March 2014. Martin Edelmann, IASB member, welcomed the GPF members. After that, Maria Theofilaktidis (new GPF member), Hugh Shields (new IASB Executive Technical Director) and Kumar Dasgupta (new IASB Technical Director) provided the group with some information about their professional backgrounds.

## IASB work plan update

2. The IASB Technical Directors gave GPF members an update on IASB's active projects.

### *Revenue recognition*

3. The new Standard on Revenue Recognition (IFRS 15) is now in production and is expected to be issued in the second quarter of 2014, with an effective date of 1 January 2017 and early application is permitted.

4. To support preparers in the initial implementation period, the IASB is planning to create, jointly with the US Financial Accounting Standards Board (FASB), a Revenue Transition Group. This group will have a limited life and will not issue authoritative guidance.

### *Insurance Contracts*

5. The comment period for the Insurance Contracts Exposure Draft ended in October 2013. During the comment period, there was extensive outreach, including fieldwork, to obtain feedback on the revised IASB proposal.

6. At its January meeting the IASB received an initial summary of the comment letters and outreach feedback. During the upcoming March meeting, the IASB will focus on the issues of unlocking the contractual service margin and

presenting changes in discount rates. The IASB plans to publish the final Standard next year, and has not yet decided the effective date.

7. The FASB has recently decided to consider making improvements to US GAAP rather than continuing to develop the model proposed in its 2012 Exposure Draft *Insurance Contracts*.

### *Financial Instruments*

8. The IASB's discussion of the Classification and Measurement project and the Impairment project finished in February 2014. The IASB expects to issue an updated IFRS 9 *Financial Instruments* in the second quarter of 2014, with an effective date of 1 January 2018. The IASB also plans to publish a Discussion Paper on Macro Hedging around the end of the first quarter of 2014.

### *Disclosure Initiative*

9. The Disclosure Initiative comprises a number of projects:

   (a) Narrow-scope amendments to IAS 1 *Presentation of Financial Statements* to clarify some issues, for example, materiality.

   (b) Materiality: the IASB is looking at how materiality is applied in practice in IFRS financial statements. The IASB will then consider whether further guidance is needed.

   (c) Principles of disclosure: the IASB is starting a project on principles of disclosures, which in practice may require also reviewing some aspects of presentation.

10. A GPF member cautioned the IASB not to extend the scope of the project on principles of disclosure. He thought that the IASB may not be able to achieve its objectives for this project if it includes all matters covered in the previous project on financial statement presentation, such as cohesiveness and direct cash flows.

### *Other projects on the IASB's work programme*

11. A GPF member asked for more details about the project on 'Clarification of acceptable methods of depreciation and amortisation'. The staff explained that

this is a planned narrow-scope amendment to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* to prohibit the use of a revenue-based depreciation or amortisation method. The IASB expected to publish the final amendment in the second quarter of 2014.

12. A GPF member commended the IASB for its active participation on integrated reporting and expressed regret that the FASB did not participate in that project.

13. A GPF member expressed disappointment that the IASB and FASB could not achieve convergence on many of the projects previously agreed to in their Memorandum of Understanding. This member thought that this reflected a lack of leadership and suggested the accounting profession should put aside their self-interest in the public interest.

## Financial instruments: expected credit loss model

14. The staff gave an update on the project on the impairment of financial instruments. This included a brief description of the model proposed in the Exposure Draft *Financial Instruments: Expected Credit Losses*, and of the feedback received on that document.

15. A GPF member was concerned about achieving consistency between financial institutions using an impairment model that is judgemental, for example when assessing impairment of some government bonds.

    (a) Martin Edelmann said the objective of the impairment model is not to make entities directly more comparable. Any expected credit loss model is highly judgmental. The objective of moving to an expected loss model is to use more forward-looking information to help users to evaluate an entity's exposure to credit risk.

16. Some GPF members raised an issue about lack of convergence with US GAAP.

    (a) The IASB's proposed impairment model for financial assets is preferable to the FASB's proposed model. The FASB's model reports a loss on Day 1 that is misleading because it does not consider the future margins that the existing financial assets will generate. However, perhaps the IASB should wait before finalising IFRS 9 until it knows

the FASB's final model, because there is still uncertainty as to what the FASB is planning. For example, one alternative the FASB is considering would take the Day 1 loss through other comprehensive income (OCI) and recycle it over the life of the instrument.

(b) It is a concern that apparently the accounting profession could not decide on a single set of requirements to account for financial instruments.

(c) Martin Edelmann noted that the IASB has finalised its discussion of impairment, after considering various models with the FASB for an extensive period. He does not expect the IASB to reopen the impairment project for further discussion.

(d) Some GPF members observed that having two separate impairment models seems rather onerous.

  (i) Regulators might require entities to calculate the loss allowance under both IFRS and US GAAP, and to treat the difference as part of required capital. That could confuse investors and analysts and increase costs to preparers.

  (ii) Financial reporting and regulatory reporting meet different needs. The IASB's impairment model is appropriate for financial reporting. Also, many regulators already require deductions in regulatory reporting for expected credit losses.

17. Wei-Guo Zhang stated that the IASB will not require extra disclosure to compensate for a lack of convergence in the recognition and measurement of impairment losses. Regulators might require such disclosure, but the IASB cannot prevent that.

18. Some GPF members made other comments:

(a) It is a concern that when an entity elects to present changes in the fair value of equity instruments in OCI, those changes will never subsequently be transferred to profit or loss (recycled). There has not been sufficient discussion on the matter.

(b) Some disclosures are ‘nice to know’ and some are ‘need to know’, but there is a problem if the information is not being used at all.

(c) The IFRS 9 project has been running long enough and it is time to complete it.

## Accounting for macro hedging

19. The staff provided an overview on the project on macro hedging. The staff also asked the GPF whether they think that the project’s considerations about dynamic risk management for interest rate risk are relevant for other types of risk (eg commodity price risk) and for entities other than banks.

20. A GPF member stated that this topic is complicated, particularly for banks. The aim of banks’ risk management is to transform, for example, fixed interest rate exposures to variable interest rate exposures. The Portfolio Revaluation Approach seeks to capture this transformation of interest rate risk. It is difficult to reach a conclusion yet, because there could be very different accounting outcomes depending on the scope of this model. If the scope is broad (eg whole banking book exposures) and the model covers not only interest rate risk but also other risks (eg credit risk), the de facto result could be a fair value model. This would lead to more volatility in profit or loss, and so banks would hesitate to provide fixed interest rate loans. That would have adverse macroeconomic impacts.

21. Martin Edelmann stated that current general hedge accounting does not work for dynamic risk management of net risk positions. He agreed that if the Portfolio Revaluation Approach is applied to the whole banking book exposure, a bank could face more profit or loss volatility if it uses derivatives than if the bank does not use derivatives for this purpose. He also mentioned, however, that if a bank’s risk management policy is to eliminate interest rate risk, the model has advantages in terms of operational feasibility. He emphasised that the Discussion Paper would carefully discuss these important issues.

22. A number of comments were raised on scope.

(a) An accounting model for macro hedging is needed for other risks and for all entities. For example, an entity may not currently be able to

achieve hedge accounting for equity risk and would face a disconnection between risk management and accounting, for example if its risk management objective is to manage exposure against an all-world index.

(b) There may also be issues relating to commodities risks and foreign exchange risk. A related issue is whether one currency could be viewed, for accounting purposes, as hedging another currency (eg New Zealand Dollar versus Australian Dollar).

(c) Accounting for macro hedging should be principle-based. Practice today is driven by accounting requirements.

23. Some GPF members also commented on the disclosure requirements resulting from the project.

(a) A GPF member asked what the disclosure consequences are. The member noted that for dynamic risk management, the 'picture' at the end of the reporting period would have changed by the time when the financial report was issued. For that reason, the member questioned whether the information would still be relevant for decision-making purposes.

(b) The staff noted that the IASB discussed quantitative and qualitative disclosures. The IASB considered that the balance sheet is a snapshot and that the disclosures should show how effective risk management was for the period under consideration. For instance, the disclosures would try to show how effective an entity has been in transforming the net interest margin before and after risk mitigation.

24. A GPF member asked how the accounting model for macro hedging relates to the Insurance Contracts project and whether the accounting model can be applied to insurers. The staff stated that because the Portfolio Revaluation Approach recognises revaluation adjustments in profit or loss, the approach would not mitigate an accounting mismatch if it arises for insurers in OCI, rather than in profit or loss. The staff mentioned that the DP would discuss an 'alternative OCI approach' but that this alternative would make it difficult to deal with internal

derivatives, for which the amounts recognised in OCI would not equal offsetting amounts recognised in profit or loss.

25. Wei-Guo Zhang said that some features of risk management, such as use of transfer pricing transactions, are common to banks and corporates and asked GPF members to give input to the IASB about how the accounting for macro hedging could be relevant for the corporate sector. He also suggested that the Portfolio Revaluation Approach has a result that is similar to using a standard costing system.

## Leases

26. The staff presented some possible simplifications to the lessee accounting proposals included in the Exposure Draft *Leases* published in May 2013 (the 2013 ED).

27. The staff then asked for the GPF's views on each of the possible simplifications detailed in the Agenda Papers, in terms of:

    (a) the relative effectiveness in reducing costs of applying the proposals in the 2013 ED; and

    (b) the effect on the information that would be provided to investors and analysts.

28. The staff noted that the feedback from GPF members would be summarised for the IASB's decision-making at its March 2014 meeting.

29. GPF members gave comments on the possible simplifications included in the agenda papers as well as overall comments on the Leases project.

### *Overall comments on the Leases project*

30. A GPF member suggested that the IASB should further develop the proposals for changes to lease accounting before taking any tentative decisions. One GPF member also stated that the IASB should comply with its own due process: if the IASB makes substantial changes from its previous proposals, it may need to consider whether another Exposure Draft is needed.

31. A GPF member stated that the scope of the new Leases Standard and the definition of a lease should be discussed further.

32. A GPF member raised a concern about what would happen if the IASB and FASB did not agree on a single leases accounting model. This could increase complexity.

### *Small-ticket leases*

33. Regarding possible simplifications for small-ticket leases held by a lessee, GPF members had mixed views as follows:

    (a) Some GPF members stated that simplifications for small-ticket leases are not needed, because of the existing materiality guidance in IFRS. However, others thought that it was difficult for US-preparers to rely on materiality.

    (b) There were mixed views on the operationality of an exemption for low-value or non-core assets.

    (c) Some GPF members stated that applying the proposed lessee requirements to portfolios of leases, rather than to individual leases, would provide cost relief but that this would vary depending on the entity's circumstances. Some asked whether separate leases under a master lease would be regarded as an individual lease or a portfolio.

    (d) Some GPF members suggested that further simplification might be possible if subsidiaries could adopt group materiality levels for their own financial statements, or if they were permitted to use the IFRS for SMEs.

    (e) Although exemptions from recognition would reduce complexity, it is important not to replace recognition with costly disclosures.

### *Lessee accounting*

34. Regarding possible simplifications for lease classification for lessees, most GPF members commenting said that lease classification based on IAS 17 *Leases* is not complex because it is familiar to preparers.

35. Some GPF members expressed views, which included:

(a) support for a dual model with lease classification based on IAS 17. Some GPF members supporting this view indicated a preference for measuring the lease liability on an undiscounted basis; and

(b) support for a single model in which a lessee would recognise a single lease expense. One GPF member would prefer any single model with no lease classification to any dual model.

### *Measurement of lease assets and lease liabilities*

36. Regarding possible simplifications for the lease term:

(a) One GPF member supported retaining reassessment requirements for significant changes to the amount of lease assets and liabilities.

(b) One GPF member suggested retaining the phrase in IAS 17 "reasonably certain", rather than "significant economic incentive", when assessing the lease term.

### *Separation of lease and non-lease components*

37. GPF members gave the following comments in response to the possible simplifications for the separation of lease and non-lease components:

(a) Separating components could be difficult for multinational entities if observable prices are not available at a local level.

(b) Stand-alone selling prices could be estimated, as decided for the Revenue Recognition project.

(c) Is IFRIC 4 *Determining whether an Arrangement contains a Lease* working? The staff responded that there was no evidence that IFRIC 4 was not working.

(d) If the lease component is small, the entire contract could be accounted for as a service contract.

(e) Separation is not necessary if one of the components is not material.

## IFRIC Update

### *Overview of the activities of the IFRS Interpretations Committee (the Interpretations Committee)*

38. The IASB staff gave an overview of the activities of the Implementation and Interpretations team. The staff also summarised some of the recent amendments to IFRSs from that team.

39. The staff encouraged members to send comments and reminded them about the Interpretations Committee's website, which includes a description of all the issues that the Interpretations Committee has analysed. GPF members could also subscribe to an email alert that informs them about the Interpretation Committee's activities.

### *Process to resolve implementation issues*

40. The staff recalled the strategic review of the Interpretations Committee's activities conducted by the Trustees in 2011. As a result of the review, the Trustees:
    (a) gave the Interpretations Committee a much broader range of tools in addition to the Annual Improvement process and the Interpretations themselves, adding narrow-scope amendments to IFRSs to its toolkit;
    (b) decided that the Interpretations Committee should have a single set of agenda criteria, including widespread relevance and divergence in practice, because of the importance of the consistency of application; and
    (c) formalised the Interpretations Committee's approach toward publicising its agenda decisions, including issues that were not taken within its agenda).

41. A GPF member suggested that these 'non-agenda' items should be aggregated on a periodic basis and bundled into a publication similar to a Discussion Paper, so that they would reach a wider audience.

42. A GPF member also had a concern that while the Interpretations Committee includes preparers, auditors and users, auditors are often able to devote much

more of their time to the Committee, which creates a risk of a natural bias in the Committee's assessments.

(a) The staff expressed a belief that more support at early stages of implementation could address this problem, because accounting firms often start to interpret the new Standards on their own, causing diversity in practice.

43. Takatsugo Ochi, IASB member, agreed that in his experience (as a former member of the Interpretations Committee), the Interpretations Committee's discussions were dominated by auditors, who have more experience of each topic than preparers do. Mr Ochi emphasised that IFRS are generally accepted principles, not detailed directions. Once the Standard is clear, divergence in practice will disappear over time. The Interpretations Committee plays a role in helping to determine whether any divergence that arises is significant or not. Consequently, the Interpretations Committee is now reaching out to standard-setters in each country to improve communication about any issues that arise.

### *Feedback on IFRIC 21* Levies

44. The staff asked GPF members to share their experience and other views on the implementation of IFRIC 21 *Levies*, issued in May 2013 as an Interpretation of IAS 37, with an effective date of 1 January 2014.

45. The staff gave some background information on IFRIC 21 and some of the comments that have arisen since publishing IFRIC 21:

(a) IFRIC 21 does not apply to contractual arrangements with the government, nor to income taxes and fines.

(b) The Interpretations Committee has received comments on some expenses that are currently recognised over time, not at a single point in time; for example, property taxes.

(c) Many comments received since IFRIC 21 was issued acknowledged the increased clarity about the credit (recognition of the liability) but

queried the accounting for the related debit, which is outside the scope of the Interpretation.

(d) Many entities now realise that the Interpretation concerns not only banking levies, but all governmental levies. It seems that currently many entities are reviewing different transactions in different jurisdictions to assess the effect of applying IFRIC 21.

46. A GPF member stated that although they are not challenging the result, they were surprised at the rationale behind it, because levies are calculated on the basis of prior year sales. This led to a lot of discussion.

(a) The activity that leads to the recognition of the liability is identified in each case in the relevant legislation. In some cases, the trigger for the levy is the generation of revenue in the current period, but the measurement of the levy is based on revenue generated in a previous period. In these cases, the trigger for recognition is not revenue generation in the previous period; the prior year activity is necessary, but is not sufficient, to create a present obligation

(b) The staff noted that this issue is also considered in the *Conceptual Framework* Discussion Paper. In relation to the criteria for identifying the obligating event, the staff summarised responses to the Discussion Paper on the *Conceptual Framework:* Alternative 1 (unconditional obligation only) had few supporters, and there was no consensus on Alternatives 2 (practically unconditional) and 3 (entity no longer has complete discretion) because respondents felt they were not described clearly enough. This area would be further developed in work toward the Exposure Draft on the *Conceptual Framework*.

47. GPF members made the following comments:

(a) Guarantees have caused problems.

(b) The conclusion leads to results in interim announcements that appear counterintuitive, because levies cover a year.

(i) The staff explained that the IASB considered and rejected creating an exception to IAS 34 to address this problem, because IAS 34 is based on the principle that transactions

should be reported in the interim period in the same way as they would be reported annually.

(c) Licences to sell pharmaceuticals often set royalties based on sales. There was a great deal of discussion in the pharmaceutical industry about whether the royalties payable, based on sales, should be considered a revenue deduction or an expense. One GPF members asked whether, by analogy, gross or net presentation had been considered in the cases when levies are based on sales.

(d) The generic examples in IFRIC 21 use very specific terminology that could be over-interpreted. The potential solution is to limit the level of detail for generic examples.

48. A GPF member suggested that some concerns about IFRIC 21 have arisen because it did not address the 'debit' side of the transaction.

(a) Philippe Danjou recalled a view presented by some audit firms that the debit should not go directly to profit and loss, because it is not a tax, but a levy. This is a form of exchange, because the entity does receive benefits, even if they are difficult to identify. However, identifying such indirect benefits may be subjective and could mean taking the Interpretation too far.

49. Other GPF members thought that the Interpretation is based on the 'legal form' of the levy rather than its 'economic substance'.

## Post-implementation review of IFRS 3 *Business Combinations*

50. The staff provided an overview of the current status of the Post-implementation Review of IFRS 3 *Business Combinations*. That review is now in Phase II, investigating the issues identified in the first phase of the project and included in the Request for Information. The objective of this session was to receive input from GPF members on the more relevant questions in the Request for Information.

### *Issue 1: Definition of a business*

51. Several GPF members suggested that the definition of a business is an issue in practice, including:

(a) More help is needed to determine what is or is not a business. An example is an acquisition of a patent portfolio, for which it can be difficult to determine whether it is an acquisition of a business or of assets.

(b) The issue arose when the definition of a business changed; in particular the word 'capable' in the definition causes problems, because it is focused on the future. One example is where a mining entity acquired a non-operating incorporated entity with a processing plant that had been mothballed and with mineral resources on an adjoining property. The acquisition was treated a business combination because the property was deemed 'capable' because economies of scale would make mining economically viable after the acquisition, even though mining was not economically viable before. The definition of a business included in the SEC's accounting Regulation is better, because is focused on the past.

(c) If the requirements for contingent consideration were changed, much of the debate about what a business is would go away. Contingent consideration is a particular concern for the pharmaceutical industry.

(d) Is a legal entity always a business?

### *Issue 2: Fair value–measurement*

52. Comments include:

(a) The guidance on pre-existing contracts is difficult to apply, because it takes a great deal of work to decide whether they are favourable or unfavourable.

(b) It is difficult to identify whether payments for continuing employment of former shareholders are part of the consideration or compensation, but it is necessary to do so and management usually knows whether they are consideration or compensation.

### *Issue 3: Separate recognition of intangible assets from goodwill*

53. Comments include:

    (a) The allocation of value is difficult; the intangible asset exists but it is difficult to measure.

    (b) The separate recognition of intangible assets with indefinite life is questionable.

    (c) Intangible assets and goodwill should be separate.

    (d) There is an incentive not to find intangible assets, because goodwill is not amortised.

### *Issue 4: Non-amortisation of goodwill and indefinite-life intangible assets*

54. Comments include:

    (a) The impairment test for goodwill is complex and time-consuming. The allocation of goodwill is easy at acquisition date, but afterwards an entity may lose the link between goodwill and the underlying operations.

    (b) Goodwill should be amortised, because the amortisation of goodwill would reduce the incentive not to find intangible assets.

    (c) Goodwill should be debited to equity on the date of the acquisition.

### *Issue 5: Non-controlling interests*

55. Comments include:

    (a) Some prefer measuring NCI at fair value when the acquirer expects to acquire or sell NCIs, because this measurement method is easier to apply when acquiring or selling NCIs. Measuring NCI proportionately to the acquiree's net assets is preferable when the acquirer does not expect to change his ownership interest in the acquiree, because in this case the goodwill is lower.

    (b) The unit price for a large block of shares is different from the unit price for the last few shares needed to acquire control. A previously held

large minority interest should not be remeasured at the price paid to acquiring the last few shares that were publicly traded.

### *Issue 6: Disclosures.*

56. Comments include:

    (a) The disclosures for business combinations should not push business decisions. For example, an acquirer may decide to delay signing the contract to purchase a business until the day after the financial statements are authorised for issue in order to not have to disclose that business combination.

    (b) Disclosures about the subsequent performance of the acquired business could be useful, but this disclosure may be difficult to provide.

    (c) Too much disclosure is required.

## Accounting in a high-inflation economy or hyperinflationary economy

57. Malcolm Cheetham gave a presentation on an issue that arises when a company consolidates a foreign subsidiary that operates in an economy that is experiencing high inflation or hyperinflation. In summary, this issue is caused by:

    (a) the requirement to consolidate foreign subsidiaries using the 'official' foreign exchange rates that do not reflect the market value in economies that are facing high inflation, eg currently in Venezuela, or are undergoing hyperinflation. This has resulted in financial performance in those subsidiaries appearing at values that are artificially inflated.

    (b) tight exchange controls.

58. GPF members made the following comments:

    (a) This issue arises for companies that invest in some Latin American companies.

(b) The IASB should allow entities:

(i) to use an exchange rate other than the 'official' exchange rates so that the results from the foreign subsidiary are comparable to other entities in the group.

(ii) to recognise an impairment loss on cash that is trapped in foreign subsidiaries by tight exchange controls and is likely to result in a significant foreign exchange loss by the time it is ultimately repaid or distributed to the parent.

59. Ian Mackintosh noted that the IASB's Emerging Economies Group had also raised issues about accounting for high inflation in its recent meeting in early 2014. The members in that group had different views on how to address this issue and what would be deemed to be the correct foreign exchange rate. He thanked Malcolm for highlighting this issue and noted that this issue would be considered as part of the IASB's research project on accounting in hyperinflationary economies.

## Conceptual Framework

### *Update on summary of comment letters*

60. The staff presented an overview of feedback from comment letters and user outreach on the IASB's Discussion Paper *A Review of the Conceptual Framework for Financial Reporting*. The comment letter period ended in February 2014, and the IASB received about 220 comment letters.

61. GPF members gave the following comments and suggestions in response to that overview:

(a) The existing Standards indirectly apply the concept of a business model (for example, in IFRS 9 *Financial Instruments*). It should be addressed in the *Conceptual Framework* (CF).

(b) Financial statements based on the business model are the best way to achieve faithful representation and the business model should be addressed in the CF. Other participants had mixed views on this issue; they thought that:

(i) The main impact of the business model is on the selection of the measurement approach. An example is whether it is useful to provide information if an entity chooses to do the work themselves or outsource it.

(ii) The business model is important but not essential, and it is difficult to develop a sound concept of a business model.

(iii) Requirements for reassessment and reclassification when the business model changes may result in complexity and less understandable information to investors/analysts.

(iv) The business model may not work if management changes.

(c) Defining profit or loss is very important and, even though it is difficult, the IASB should prioritise the development of such a definition.

(d) With regard to the feedback that many respondents preferred a broad approach to determining what is included in other comprehensive income (OCI), but had not supported the suggested categories in the Discussion Paper: the reason for this response was that those categories would not rationalise the calculation of earnings per share (EPS).

62. Some GPF members asked the staff about the substance of feedback received in the comment letters.

(a) The staff thought that the level of responses was helpful. However, in some areas (for example, definition of P&L, distinction between equity and liabilities, three suggested categories of OCI) few respondents had made suggestions for better approaches, even though they had apparently not been convinced by the Discussion Paper's approach to those areas.

### *Status and purpose of CF*

63. The staff noted that the DP suggested that the primary purpose of the CF is to help the IASB develop Standards, but the feedback indicates that other parties use it as well. The purpose of this session was to find out how often preparers use the CF.

64. GPF members made the following comments and suggestions:

(a) Some GPF members agreed that the purpose of the CF should be to help the IASB develop Standards. They stated that preparers do not use it much.

(b) Some GPF members said that even though they may not use the CF often, they want it as a point of reference. Examples of applying the CF included:

(i) going back to the definitions and recognition criteria when some issue is unclear;

(ii) if they think that a Standard goes into too much detail or results in an intuitively unsuitable outcome, they would review the guidance in the CF. They do not use the CF as an override. They cannot ignore the Standard if the CF seems to say something different, but when there is a choice, the CF may support one of the options;

(iii) when writing comment letters; and

(iv) when preparing the company's internal implementation guidance on accounting standards (for example how to apply IFRS 3 to identify assets and liabilities acquired in a business combination).

(c) Most participants stated that it is difficult to base a decision on the CF. They prefer using other sources such as national accounting requirements in other jurisdictions or accounting manuals produced by the accounting firms.

(d) Some respondents thought that if the CF was more developed, they would use it more.

### *Case studies on the updated definition/recognition criteria in rate-regulated activities*

65. One of the issues that the IASB is seeking to address in its Rate-regulated Activities project is whether some types of rate regulation create assets or liabilities in particular circumstances. GPF members were asked whether the

same assets or liabilities would arise in other industries in the examples used in the staff paper.

66. The staff paper had three examples faced by many rate-regulated entities:

    (a) when a change of allowable input costs in the current year causes an automatic change in the rate for the subsequent year;

    (b) when, as a result of fulfilling the requirements to improve/maintain quality of service, a bonus or a penalty is incorporated in the rate for the subsequent year; and

    (c) when a regulator guarantees the recovery of repair costs due to storm damage after the event. Alternatively, the regulator can build into the rate an advance recovery of an estimate of future repair costs (but then the rate may have to be reduced if a storm does not happen).

67. GPF members made the following comments:

    (a) GPF members had mixed views on whether an asset or liability could arise in those situations:

        (i) Some GPF members thought that, taking into account all the assumptions specified in the examples, an entity would have an asset or a liability. The resource is the promise by the regulator that the entity can increase the future rate. The regulator is compelled to ensure that there is electricity supply, and thus the entity has a guaranteed receipt. These GPF members distinguished the economic resource, which is the promise, from the expected future cash flows, which are the payments that are due to be made later. They thought that an entity had an asset or liability whether applying the old or the new definitions (expected vs capable).

        (ii) However, one member thought that in order to earn revenue one needs to produce electricity and sell it, so that member did not recommend recognising any of those anticipated costs as assets or liabilities because they are conditional on future production.

(iii) Another member thought that the revenue related to anticipated costs, such as future storm costs, should be considered as deferred revenue.

(iv) Companies operating in other industries do not have such guarantees from regulators, so they would not have the assets.

(v) The GPF members discussed whether enforceability of the contract with the regulator would affect whether assets or liabilities could arise. They mentioned that in some countries, eg South Africa, the regulators sometimes change the terms of their guarantees. In the US the rate-regulated entities had gone bankrupt, thus undermining the validity of those guarantees.

(b) Some GPF members thought that the contract was between the regulator and the rate-regulated entity. The contact only relied on consumers to buy electricity as a form of payment.

(c) A GPF member noted that many energy distributors in Brazil were unhappy that they were unable to apply the exception that is now allowed in IFRS 14. When they had first adopted IFRS, they had to write off their regulatory assets.

(d) One GPF member thought that the concept of prudence was applicable in the rate-regulated activities situation. Consequently, in Example 1, the entity should not recognise an asset, because it is difficult to reasonably estimate it. This is because it depends on the next year’s sales. However, the entity should recognise a liability if it is reasonably estimable. The member thought that entities should apply a higher level of probability for an asset than for a liability.

(e) One GPF member did not think that an asset or liability would arise in Example 3b, because it would be akin to predicting a storm that may or may not happen.