

IFRIC[®] Update

From the IFRS[®] Interpretations Committee



May 2016

Welcome to the IFRIC Update

IFRIC Update is a summary of the tentative decisions reached by the IFRS Interpretations Committee (Interpretations Committee) in its public meetings. All conclusions reported are tentative and may be changed or modified at future Interpretations Committee meetings.

Decisions become final only after the Interpretations Committee has taken a formal vote on an Interpretation or a Draft Interpretation, which is then confirmed by the International Accounting Standards Board (the Board).

The Interpretations Committee met in London on **10 May 2016**, and discussed:

- **Items on the current agenda**
- [IFRS 9 *Financial Instruments* and IAS 28 *Investments in Associates and Joint Ventures*—Measurement of long-term interests \(Agenda Paper 2\)](#)
- [IAS 12 *Income Taxes*—Expected manner of recovery of indefinite life intangible assets when measuring deferred tax \(Agenda Paper 10\)](#)
- [IAS 21 *The Effects of Changes in Foreign Exchange Rates*—Foreign Currency Transactions and Advance Consideration \(Agenda Paper 7–7B\)](#)
- **Deliberation of comments received on proposed narrow-scope amendments**
- [IAS 40 *Investment Property*—Exposure Draft of proposed amendments to IAS 40 *Transfers of Investment Property* \(Agenda Paper 5\)](#)
- **Interpretations Committee’s tentative agenda decisions**
- [IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*—Fees and costs included in the ‘10 per cent’ test for the purpose of derecognition \(Agenda Paper 11\)](#)
- [IAS 32 *Financial Instruments: Presentation*—Accounting for a written put option over non-controlling interests to be settled by a variable number of the parent’s shares \(Agenda Paper 9\)](#)
- [IFRIC 12 *Service Concession Arrangements*—Accounting for service concession arrangements for which the infrastructure is leased \(Agenda Paper 4\)](#)
- **Interpretations Committee’s agenda decisions**
- [IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*—Derecognition of modified financial assets \(Agenda Paper 6\)](#)
- [IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*—Accounting for repayable cash receipts \(Agenda Paper 3\)](#)
- [IAS 36 *Impairment of Assets*—Recoverable amount and carrying amount of a cash-generating unit \(Agenda Paper 8\)](#)
- **Other matters**
- [Interpretations Committee work in progress update \(Agenda Paper 12\)](#)

Contact us

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

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

Future IFRS Interpretations Committee meetings

The next meetings are:

12 July 2016
6 and 7 September 2016
8 and 9 November 2016

Meeting dates, tentative agendas and additional details about the next meeting will be posted to the IFRS [website](#) before the meeting. Further information about the activities of the IFRS Interpretations Committee can be found [here](#). Instructions for submitting requests for Interpretations are given on the IFRS website [here](#).

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Items on the current agenda

At this meeting, the Interpretations Committee discussed the following items on its current agenda:

IFRS 9 *Financial Instruments* and IAS 28 *Investments in Associates and Joint Ventures*—Measurement of long-term interests (Agenda Paper 2)

The Interpretations Committee received a request relating to the interaction between IFRS 9 *Financial Instruments* and IAS 28 *Investments in Associates and Joint Ventures*. Specifically, the issue relates to whether an entity applies IFRS 9, IAS 28 or a combination of both Standards to the measurement of long-term interests in an associate or a joint venture that, in substance, form part of the net investment in the associate or joint venture, but to which the equity method is not applied (long-term interests).

The Interpretations Committee observed that:

- a. paragraph 14 of IAS 28 clarifies that the scope exception in paragraph 2.1(a) of IFRS 9 applies only to interests in an associate or a joint venture that an entity accounts for using the equity method; and
- b. long-term interests are not accounted for using the equity method. This is because:
 - i. paragraph 38 of IAS 28 distinguishes between the investment in an associate or a joint venture determined using the equity method and any long-term interests that in substance form part of the entity's net investment in the associate or joint venture; and
 - ii. long-term interests are subject to only one part of the equity-method procedures—the allocation of losses.

Consequently, on the basis of an analysis of the requirements in IAS 28 and IFRS 9, the Interpretations Committee noted that the scope exception in paragraph 2.1(a) of IFRS 9 does not apply to long-term interests.

The Interpretations Committee observed the following:

- a. an entity accounts for long-term interests applying IFRS 9, including the impairment requirements in IFRS 9;
- b. in allocating any losses of the associate or joint venture applying the requirements in paragraph 38 of IAS 28, the entity includes the carrying amount of those long-term interests (determined applying IFRS 9) as part of the net investment to which the losses are allocated;
- c. the entity then assesses for impairment the net investment in the associate or joint venture, of which the long-term interests are a part, by applying the requirements in paragraphs 40 and 41A–43 of IAS 28; and
- d. if an entity allocates losses or recognises impairment applying steps (b) and (c) above, the entity ignores those losses or that impairment when it accounts for long-term interests applying IFRS 9 in subsequent periods.

The Interpretations Committee noted that the feedback from outreach activities indicated that there are diverse reporting methods applied to account for long-term interests and that the issue is widespread. Consequently, the Interpretations Committee tentatively decided to develop a draft Interpretation, which would explain how to account for long-term interests.

Next steps

The staff will prepare a draft Interpretation.

IAS 12 *Income Taxes*—Expected manner of recovery of indefinite life intangible assets when measuring deferred tax (Agenda Paper 10)

The Interpretations Committee received a request to clarify the determination of the expected manner of recovery of an indefinite-life intangible asset for the purposes of measuring deferred tax.

The Interpretations Committee observed that, when measuring deferred tax on indefinite-life intangible assets, an entity applies paragraphs 51 and 51A of IAS 12 in reflecting the tax consequences that follow from the expected manner of recovery of the carrying amount of those assets. However, during the discussion, an Interpretations Committee member suggested that the Interpretations Committee could go further in clarifying how to determine the expected manner of recovery in this situation by exploring the interaction between how

an asset is amortised and the requirements in paragraphs 51 and 51A of IAS 12.

Next steps

The Interpretations Committee will consider this issue further at a future meeting.

IAS 21 *The Effects of Changes in Foreign Exchange Rates—Foreign Currency Transactions and Advance Consideration* (Agenda Paper 7–7B)

The Interpretations Committee considered a summary of the comment letters to the draft Interpretation *Foreign Currency Transactions and Advance Consideration*, and commenced its redeliberations of the proposals in the draft Interpretation.

The Interpretations Committee tentatively decided to retain in the final Interpretation the following proposals in the draft Interpretation:

- a. the scope, explaining in the Basis for Conclusions:
 - i. why an entity is not required to apply the Interpretation to insurance contracts and income taxes; and
 - ii. that determining whether an item is non-monetary depends on the particular facts and circumstances, and may require judgement;
- b. the consensus; and
- c. the transition requirements.

The Interpretations Committee also tentatively decided to provide first-time adopters of IFRS Standards with the same transition relief as is provided to entities already applying IFRS Standards.

Next steps

The Interpretations Committee will finalise its redeliberations of the draft Interpretation at a future meeting.

Deliberation of comments received on proposed narrow-scope amendments

IAS 40 *Investment Property—Exposure Draft of proposed amendments to IAS 40 *Transfers of Investment Property (Agenda Paper 5)**

The Interpretations Committee considered a summary of the comment letters to the Exposure Draft *Transfers of Investment Property* (Proposed amendments to IAS 40), and discussed the proposals in the Exposure Draft.

The Interpretations Committee recommended to the Board that it should proceed with the proposed amendments to IAS 40, subject to the following:

- a. clarifying in paragraph 57 of IAS 40 that a change in management's intentions, in isolation, does not provide evidence of a change in use;
- b. amending two of the examples in paragraph 57 of IAS 40 so that they could relate to property under construction or development as well as completed property; and
- c. emphasising, in the Basis for Conclusions, that judgement may be required to assess whether a property meets, or has ceased to meet, the definition of investment property.

The Interpretations Committee also recommended that an entity be permitted to apply either of the following transition approaches when first applying the proposed amendments to IAS 40:

- a. a full retrospective approach in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
- b. an approach for which the entity:
 - i. would reassess the classification of property to reflect its use at the date of transition; and
 - ii. would apply the proposed amendments to changes in use that occur after the date of transition.

Next steps

The Board will discuss the Interpretations Committee's recommendations at a future Board meeting.

Interpretations Committee's tentative agenda decisions

The Interpretations Committee reviewed the following matters and tentatively decided that they should not be added to its agenda. These tentative decisions, including recommended reasons for not adding the item to the Interpretations Committee's agenda, will be reconsidered at a future Interpretations Committee meeting. Interested parties who disagree with the proposed reasons, or believe that the explanations may contribute to divergent practices, are encouraged to email those concerns by 22 July 2016 to ifric@ifrs.org. Correspondence will be placed on the public record unless the writer requests confidentiality, supported by good reason, such as commercial confidence.

IFRS 9 Financial Instruments and IAS 39 Financial Instruments: Recognition and Measurement—Fees and costs included in the '10 per cent' test for the purpose of derecognition (Agenda Paper 11)

The Interpretations Committee received a request to clarify the requirements in IAS 39 and IFRS 9 relating to which fees and costs should be included in the '10 per cent' test for the purpose of derecognition of a financial liability.

The Interpretations Committee observed the following:

- a. paragraphs AG62 of IAS 39 and B3.3.6 of IFRS 9 require an entity to include 'any fees paid net of any fees received' in the '10 per cent' test when assessing whether the terms of an exchange or a modification of a financial liability are substantially different and lead to the derecognition of the original financial liability. Those paragraphs also include requirements regarding how to account for 'any costs or fees incurred' relating to the exchange or modification depending on whether that exchange or modification led to the derecognition of the financial liability.
- b. in considering the items to include in the calculation of the effective interest rate, IAS 39 and IFRS 9 distinguish between 'fees and points paid or received between the parties to the contract' and 'transaction costs'. The Interpretations Committee noted that the objective of the '10 per cent' test is to quantitatively assess the significance of any difference between the old and new contractual terms by analysing the effect of the changes in the contractual cash flows (ie the contractual cash flows between the lender and the borrower). Consequently, the 'fees' included in the '10 per cent' test are similar to the 'fees and points paid or received between the parties to the contract' included in the calculation of the effective interest rate. In contrast, 'any costs or fees' incurred relating to an exchange or a modification have a similar nature to 'transaction costs' in that they are incremental costs directly attributable to the exchange or modification. Those costs or fees would not have been incurred if the entity had not exchanged or modified the financial liability.

On the basis of these observations, the Interpretations Committee noted that, when applying paragraphs AG62 of IAS 39 and B3.3.6 of IFRS 9 in carrying out the '10 per cent' test, an entity includes only fees paid or received between the lender and the borrower or fees paid by, or on behalf of, the lender or the borrower.

In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

IAS 32 Financial Instruments: Presentation—Accounting for a written put option over non-controlling interests to be settled by a variable number of the parent's shares (Agenda Paper 9)

The Interpretations Committee received a request regarding how an entity accounts for a written put option over non-controlling interests (NCI put) in its consolidated financial statements. The NCI put has a strike price that will, or may, be settled by the exchange of a variable number of the parent's own equity instruments.

Specifically, the Interpretations Committee was asked to consider whether, in its consolidated financial statements, the parent recognises:

- a. a financial liability representing the present value of the option's strike price—in other words, a gross liability; or

- b. a derivative financial liability presented on a net basis measured at fair value.

The Interpretations Committee was also asked whether the parent applies the same accounting for NCI puts for which the parent has the choice to settle the exercise price either in cash or a variable number of its own equity instruments to the same value.

The Interpretations Committee observed that in the past it had discussed issues relating to NCI puts that are settled in cash. Those issues were referred to the Board and are being considered as part of the Financial Instruments with Characteristics of Equity (FICE) project.

The Interpretations Committee noted that:

- a. on the basis of its previous discussions, it would be unable to resolve the issue without expanding the scope of the issue to a broader range of similar arrangements. Consequently, the issue is too broad for the Interpretations Committee to address efficiently within the confines of existing IFRS Standards and the Conceptual Framework; and
- b. the Board is currently considering the requirements for all derivatives on an entity's own equity comprehensively as part of the FICE project.

For these reasons, the Interpretations Committee [decided] not to add this issue to its agenda.

IFRIC 12 *Service Concession Arrangements*—Accounting for service concession arrangements for which the infrastructure is leased (Agenda Paper 4)

The Interpretations Committee received a request to clarify how an operator accounts for a service concession arrangement for which the infrastructure is leased. In this arrangement, the operator is not required to provide any construction or upgrade services with respect to the infrastructure.

The submitter described an arrangement that involves three parties: a grantor, an operator and a lessor. The operator enters into an arrangement with the grantor to operate a public service. The infrastructure in the arrangement is leased from the lessor. The lessor and the grantor may be controlled by the same governmental body. The operator is contractually required to pay the lessor for the lease of the infrastructure. The operator has an unconditional contractual right to receive cash from the grantor to reimburse those payments. In arrangements in which the lessor and the grantor are not controlled by the same governmental body, the grantor provides a guarantee of the lease payments to be made during the lease term, and of any residual value at the end of the lease term. The grantor also has an option to renew the lease at the end of the initial non-cancellable period of the contract.

The submitter asked the Interpretations Committee to clarify whether the arrangement is within the scope of IFRIC 12 *Service Concession Arrangements* (scope issue). If the arrangement is within the scope of IFRIC 12, the submitter notes that the lease of the infrastructure is not within the scope of IFRS 16 *Leases* (IAS 17 *Leases*) for the operator. Consequently, the submitter also asked the Interpretations Committee to clarify how the operator accounts for any assets and liabilities arising from the arrangement with the lessor (recognition and presentation issues).

With respect to the scope issue, the Interpretations Committee observed that:

- a. assessing whether a particular arrangement is within the scope of IFRIC 12 requires consideration of all facts and circumstances. In particular, the operator assesses whether the control conditions in paragraph 5 of IFRIC 12 and the condition relating to the infrastructure in paragraph 7 of IFRIC 12 apply; and
- b. the operator is not required to provide construction or upgrade services with respect to the infrastructure for the arrangement to be within the scope of IFRIC 12.

With respect to the recognition and presentation issues, if the arrangement described in the submission is within the scope of IFRIC 12, the Interpretations Committee observed that it is the grantor, and not the operator, that controls the right to use the infrastructure. Accordingly, the Interpretations Committee observed that:

- a. the operator assesses whether it is obliged to make payments to the lessor for the lease or whether the grantor has this obligation. This assessment requires consideration of all facts and circumstances. If the grantor is obliged to make payments to the lessor, then in that case the operator is collecting cash from the grantor that it remits to the lessor on the grantor's behalf.
- b. if the operator is obliged to make payments to the lessor as part of the service concession arrangement,

then the operator recognises a liability for this obligation when it is committed to the service concession arrangement and the infrastructure is made available by the lessor. At the time the operator recognises the liability, it also recognises a financial asset because the operator has a contractual right to receive cash from the grantor to reimburse those payments.

- c. the operator's liability to the lessor described in (b) above is a financial liability. Accordingly, the operator offsets the liability to make payments to the lessor against the corresponding receivable from the grantor only when the criteria for offsetting a financial asset and a financial liability in IAS 32 *Financial Instruments: Presentation* are met.

The Interpretations Committee noted that the requirements in IFRS Standards provide an adequate basis to enable an entity to determine how to account for the arrangement.

In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

Interpretations Committee's agenda decisions

IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*—Derecognition of modified financial assets (Agenda Paper 6)

The Interpretations Committee discussed whether to undertake a potential narrow-scope project to clarify the requirements in IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement* about when a modification or exchange of financial assets results in derecognition of the original asset.

Many Interpretations Committee members observed that, in their experience, the circumstances in which an entity should derecognise financial assets that have been modified or exchanged is an issue that arises in practice. However, because of the broad nature of the issue, the Interpretations Committee noted that it could not resolve it in an efficient manner. Consequently, the Interpretations Committee decided not to further consider such a project.

IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*—Accounting for repayable cash receipts (Agenda Paper 3)

The Interpretations Committee received a request to clarify the accounting for cash received from a government to help an entity finance a research and development project. More specifically, the request asked whether the entity must recognise the cash received as a liability (on the basis that the entity has received a forgivable loan as defined in IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*) or in profit or loss (on the basis that the entity has received a government grant as defined in IAS 20). The cash received from the government is repayable in cash only if the entity decides to exploit and commercialise the results of the research phase of the project. The terms of that repayment can result in the government receiving as much as twice the amount of the original cash proceeds if the project is successful. If the entity decides not to exploit and commercialise the results of the research phase, the cash received is not repayable in cash, but instead the entity must transfer to the government the rights to the research.

The Interpretations Committee noted that, in this arrangement, the entity has obtained financing for its research and development project. The Interpretations Committee observed that the cash receipt described in the submission gives rise to a financial liability (applying paragraph 20(a) of IAS 32 *Financial Instruments: Presentation*) because the entity can avoid a transfer of cash only by settling a non-financial obligation (ie by transferring the rights to the research to the government). The entity accounts for that financial liability applying IFRS 9 *Financial Instruments* (IAS 39 *Financial Instruments: Recognition and Measurement*).

The Interpretations Committee noted that, in the arrangement described in the submission, the cash received from the government does not meet the definition of a forgivable loan in IAS 20. This is because, in this arrangement, the government does not undertake to waive repayment of the loan, but rather to require settlement in cash or by transfer of the rights to the research.

The Interpretations Committee noted that, applying paragraph B5.1.1 of IFRS 9 (paragraph AG64 of IAS 39), the entity assesses at initial recognition whether part of the cash received from the government is for something other than the financial instrument. For example, in the fact pattern described in the submission, part of the cash received (the difference between the cash received and the fair value of the financial liability)

may represent a government grant. If this is the case, the entity accounts for the government grant applying IAS 20.

The Interpretations Committee noted that the requirements in IFRS Standards provide an adequate basis to enable an entity to account for the cash received from the government.

In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee decided not to add this issue to its agenda.

IAS 36 *Impairment of Assets*—Recoverable amount and carrying amount of a cash-generating unit (Agenda Paper 8)

The Interpretations Committee received a request to clarify the application of paragraph 78 of IAS 36 *Impairment of Assets*. This paragraph sets out the requirements for considering recognised liabilities in determining the recoverable amount of a cash-generating unit (CGU) within the context of an impairment test for a CGU.

The submitter questioned the approach set out in paragraph 78 of IAS 36, which requires an entity to deduct the carrying amount of any recognised liabilities in determining both the CGU's carrying amount and its value in use (VIU). The submitter asked whether an alternative approach should be required.

The Interpretations Committee observed that when an entity needs to consider a recognised liability to determine the recoverable amount of a CGU (which may occur if the disposal of a CGU would require the buyer to assume the liability), paragraph 78 of IAS 36 requires the entity to deduct the carrying amount of the recognised liability in determining both the CGU's carrying amount and its VIU. This approach of determining both the CGU's carrying amount and its VIU by deducting the same carrying amount of the recognised liability makes the comparison between the CGU's carrying amount and the CGU's recoverable amount meaningful.

The Interpretations Committee observed that the approach in paragraph 78 of IAS 36 for considering recognised liabilities provides a straightforward and cost-effective method to perform a meaningful comparison of the measures involved in an impairment test for a CGU.

In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee decided not to add this issue to its agenda.

Other matters

Interpretations Committee work in progress update (Agenda Paper 12)

The Interpretations Committee received a report on one ongoing issue and five new issues for consideration at future meetings. The report also included one issue that is on hold and that will be considered again at a future meeting.

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