

Summary note of the Accounting Standards Advisory Forum

Held on 28 September 2017 at the IASB office, 30 Cannon Street, London.

This note is prepared by staff of the International Accounting Standards Board (the Board), and summarises the discussion that took place with the Accounting Standards Advisory Forum (ASAF).¹ A full recording of the meeting is available on the IFRS Foundation[®] website.

ASAF members attending

Andreas Barckow	Accounting Standards Committee of Germany (DRSC)
Alexsandro Broedel Lopes	Group of Latin American Standard-Setters (GLASS)
Kim Bromfield	South African Financial Reporting Standards Council (SAFRC)
Yu Chen	China Accounting Standards Committee (CASC)
Patrick de Cambourg	Autorité des normes comptables (ANC)
Alberto Giussani	Organismo Italiano di Contabilità (OIC)
Russ Golden	Financial Accounting Standards Board (FASB)
Yasunobu Kawanishi	Accounting Standards Board of Japan (ASBJ)
Eui-Hyung Kim	Asian-Oceanian Standard-Setters Group (AOSSG)
Linda Mezon	Accounting Standards Board of Canada (AcSB)
Kris Peach/Kimberley Crook	Australian Accounting Standards Board (AASB) / New Zealand Accounting Standards Board (NZASB)
Andrew Watchman	European Financial Reporting Advisory Group (EFRAG)

Primary Financial Statements – Alternative Performance Measures: A New Zealand user-needs survey

1. The NZASB/AASB member summarised the findings of a survey conducted in New Zealand to determine whether external users of company reports find Alternative Performance Measures (APMs) useful. In summary, the report identified that users think APMs are useful and that the majority use APMs together with measures defined by accounting standards ('GAAP measures'). However, many users use APMs cautiously and say that APMs must be accompanied by a reconciliation to

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GAAP measures and by other explanatory information. Users also suggested some improvements to accounting standards.

2. In response to questions, the NZASB/AASB member clarified that:
 - (a) the New Zealand Financial Markets Authority has published guidance on the presentation of APMs outside the financial statements, but the NZASB does not provide additional guidance on the presentation of information in IFRS financial statements.
 - (b) there is currently variation in practice on whether APMs are included in financial statements in New Zealand, including variation in how much information is presented in the statement(s) of financial performance. In addition, some entities have gone through an exercise to remove irrelevant information from their financial statements ('cutting the clutter'); other entities have not.
 - (c) for the survey, measures presented in the primary financial statements were not considered APMs, because the authors assumed such measures met the requirements of IAS 1 *Presentation of Financial Statements*. Some entities present measures such as EBITDA (earnings before interest, tax, depreciation and amortisation) in the statement(s) of financial performance.
 - (d) no users commented on other comprehensive income.
3. Some ASAF members said the results of the survey were consistent with the findings of similar research and outreach conducted in their jurisdictions. Nevertheless, some members highlighted differences with their jurisdictions:
 - (a) the AcSB member said they are not aware of any users in Canada that use only a GAAP measure as the primary indicator of performance, whereas 20.7% of the respondents to the New Zealand survey say they do. She added that the AcSB is also doing work on APMs.
 - (b) the FASB member added that in the US they have heard that users have more confidence in APMs that are adjusted by amounts determined in accordance with US GAAP (eg measures that exclude share-based payment expenses) than in APMs that are calculated using alternative recognition and measurement criteria set by management. The DRSC member

expressed concerns about the latter category of APMs and said that such measures are difficult to reconcile to IFRS measures. He said that preparers sometimes present such measures when they disagree with the timing prescribed by accounting standards for the recognition of income or expenses (eg for banking levies) and added that such measures should not be presented with undue prominence. The NZASB/AASB member said the survey did not distinguish in this way between different types of APMs.

- (c) the SAFRC member expressed concerns about current practice in South Africa, where regulatory guidance is less strict than in New Zealand and allows entities to choose to use only APMs when communicating information about their performance in the press.
4. Some ASAF members expressed their support for some of the improvements to accounting standards suggested by the survey respondents, such as standardised definitions for some performance measures and non-recurring items. However, other ASAF members said that the Board should carefully consider the feasibility of the suggestions:
- (a) the FASB, AcSB and OIC members said that some performance measures cannot be defined consistently across all industries. The FASB member said that, for this reason, the FASB is focusing on improving disaggregation, rather than on defining performance measures. The AcSB member said that some standardisation within industries can be useful, but this may need to be addressed by other parties such as local regulators or standard-setters, rather than the Board.
 - (b) the AcSB member said the Board should not attempt to define non-recurring items. The CASC member said it is difficult to define non-recurring items and suggested using a principle-based definition.
5. Hans Hoogervorst (chairman) said the Board is currently focusing on exploring whether EBIT (earnings before interest and tax) can be defined across a range of industries to improve comparability and whether disaggregation can be improved.
6. Some ASAF members commented on the relationship between the APMs entities use to communicate externally about their performance and the performance measures they use for internal decision-making and present externally in segment reporting.

The NZASB/AASB member noted that the New Zealand Financial Markets Authority's guidance says such measures are expected to be consistent with each other. However, the FASB member said there may be differences in practice. He also said the FASB has added a project on operating segments to its agenda.

Primary Financial Statements – Feedback on the FRC Discussion Paper

7. The purpose of this session was to elicit members' views on the implications for the Board's project on Primary Financial Statements of the UK Financial Reporting Council's Discussion Paper *Improving the Statement of Cash Flows* (the FRC DP), including the responses received. Andrew Lennard from the UK FRC presented the feedback on the FRC DP.
8. Some ASAF members said that the FRC DP and the feedback received have highlighted areas in need of improvement, thereby providing useful input for the Board's Primary Financial Statements project.
9. The GLASS member said that the FRC DP does not address how to improve the usefulness of the statement of cash flows for financial institutions, which he considers an important issue. Andrew Lennard replied that the FRC did not want to duplicate work being undertaken on this topic by other organisations, such as EFRAG, or confuse the debate.
10. The SAFRC member said the reporting of notional cash flows in the statement of cash flows should not be ruled out. Whether notional cash flows are reported should depend on the objective of the statement of cash flows and to what extent 'substance over form' is applied. For example, should the statement of cash flows portray the leasing of equipment in a similar way to the portrayal of borrowing to purchase equipment? Andrew Lennard replied that in the statements of financial performance and financial position, such transactions are presented similarly. However, he expressed his opinion that the role of the statement of cash flows is to show that the related cash flows are different.
11. Some ASAF members supported the targeted improvements to the statement of cash flows that the Board has tentatively decided to consider (in paragraph 5 of [Agenda Paper 2C](#)), however:

- (a) the EFRAG, ASBJ and CASC members said the targeted improvements will depend on the Board successfully defining a comparable operating performance measure (such as EBIT) in the statement(s) of financial performance.
 - (b) the EFRAG and NZASB/AASB members noted that some respondents would like the Board to define ‘operating activities’. However, defining ‘operating activities’ positively rather than as a residual is likely to be difficult.
 - (c) the NZASB/AASB member said that eliminating the classification options for interest and dividends may be difficult, and suggested the Board could provide principle-based guidance to achieve greater consistency, rather than eliminate the options. The CASC noted the Board has so far tentatively decided to eliminate the classification options, but has not yet specified the applicable categories for interest and dividends.
12. The NZASB/AASB member said that many entities in Australia and New Zealand use the direct method, which many users prefer. Hence, she would not support eliminating the direct method. In contrast, the OIC member said he has heard from users they prefer the indirect method.
13. The NZASB/AASB member said a reconciliation—either in the primary financial statements or in the notes—between cash flows from operating activities and profit or loss is already required in Australia and New Zealand. She would support having a similar requirement in IFRS Standards.
14. The CASC member reported mixed views from their constituents on whether cash outflows to acquire property, plant and equipment should be classified as cash outflows from operating activities rather than investing activities. The OIC member queried whether any respondents suggested replacement capital expenditure should be reported as a cash outflow from operating activities, while expansion capital expenditure should be reported as a cash outflow from investing activities. Andrew Lennard said some respondents had suggested this, although others had said that making the distinction between replacement and expansion is difficult in practice.
15. The AOSSG member noted that the UK FRC received only four comment letters from users and asked whether the UK FRC would conduct further user outreach on

improving the statement of cash flows. Andrew Lennard replied that they are not planning any further activities in this area and that those four comment letters were submitted by user member groups, so they reflect the views of many users.

Rate-regulated Activities

16. At this meeting, ASAF members received an update on recent Board discussions about a possible new accounting model for activities subject to ‘defined rate regulation’ (the model).
17. ASAF members discussed illustrative examples, exploring issues that need to be considered before selecting a measurement basis for regulatory assets and regulatory liabilities. The examples focused on a regulatory asset that arises when an entity incurs costs as it delivers regulated services to customers. In accordance with the regulatory agreement the entity has a right to increase the future rate charged to customers, to the extent needed to recover those costs.
18. Most ASAF members commented that if a regulatory asset will be recovered over an extended period, the time value of money should be considered if the effect of the time value of money is material. The discussion then focussed on three main areas:
 - (a) What is the nature of the asset?
 - (b) If discounting is used, what is the appropriate discount rate to use? and
 - (c) If the initial measurement of the asset results in a ‘day one’ gain or loss, should that gain or loss be recognised immediately in the statement(s) of performance or should it be recognised systematically over time?
19. The purpose of the discussion was to identify the factors to consider when answering these questions. The factors identified by ASAF members are set out below.

What is the nature of the asset?

20. Several ASAF members suggested considering the nature of the past event that triggers the recognition of the regulatory asset, to determine whether any profit should be included in the measurement of the regulatory asset.
21. These ASAF members thought:

- (a) if the regulatory asset arises because the entity has delivered goods or services, it is like a receivable or contract asset identified in IFRS 15 *Revenue from Contracts with Customers*. In such cases, any profit attributable to the delivery performance should be recognised in the statement(s) of financial performance in the period when delivery occurs. Any financing element of the future regulated rate (price) to be charged to customers would then need to be considered separately (see below).
 - (b) if the entity incurs costs by carrying out an activity that has not yet resulted in the delivery of goods or services, the resulting regulatory asset seems more like an ‘asset from costs incurred to fulfil a contract’ asset, in IFRS 15. In such cases, a cost-based measurement approach could be more appropriate, without adjusting for the time value of money.
22. However, the NZASB/AASB member commented that given the rationale provided for recognising the asset and how it has been described in the model (as a right to increase the rate charged to customers, to the extent needed to recover the costs incurred), this suggests that the past event that resulted in recognition of the asset is not relevant to its nature or its measurement.

What is the appropriate discount rate?

23. If an entity will recover a regulatory asset only over an extended period, the rate charged to customers will often include a financing element, typically using an interest rate or rate of return set by the rate regulator. If a measurement basis involves discounting, ASAF members suggested that factors to consider when identifying an appropriate discount rate include the prevailing market interest rate, the risks associated with the regulatory asset—both financial risks and future performance risk, inflation, and returns expected by investors.
24. Some ASAF members (including the DRSC, ANC and FASB members) raised concerns about operational challenges in identifying an appropriate discount rate. They questioned whether discounting was essential.

Should any ‘day one’ gain or loss be recognised immediately or be recognised systematically over time?

25. ASAF members noted that if the asset is measured using a discount rate other than the rate set by the rate regulator, a ‘day one’ gain or loss will arise. If there is sufficient

evidence of the asset being impaired, it may be appropriate to recognise the loss immediately (irrespective of whether the regulatory asset is like a receivable, contract asset or an asset arising from costs incurred to fulfil a contract).

26. Some ASAF members stated that in some cases it is not clear what a day one loss or gain represents, such as when the calculation of a 'prevailing market rate' is subjective. They suggested that in such cases it may be more appropriate to recognise the gain or loss on a systematic basis over time.
27. The FASB member suggested that using a discount rate different from the rate set by the regulator and recognising any gain or loss systematically over time may introduce unnecessary complexities into the model, resulting in unclear information for users. An alternative would be to measure the regulatory asset using the discount rate set by the rate regulator and provide clear information about the regulatory rate of interest or return, together with information about the outstanding balance to which that rate is applied and the period over which it is applied.

Definition of a Business

28. The objective of this session was to obtain feedback from ASAF members on the Board's tentative decisions made at its April and June 2017 meetings, in the light of comments received on the Exposure Draft *Definition of a Business and Accounting for Previously Held Interests* published in June 2016. The staff was specifically seeking ASAF members' views on the differences between the Board's tentative decisions and the FASB Amendments relating to the definition of a business.
29. The ASBJ and GLASS members raised a concern on the Board's tentative decision to make the screening test optional. They were concerned that if the screening test produces an outcome that the entity does not like, the entity could state that it did not perform the screening test. They would prefer a mandatory screening test.
30. The EFRAG member expressed the same concerns as the ASBJ and GLASS members. He stated that he would prefer to change the screening test to an indicator or a rebuttable presumption. The AASB/NZASB member also preferred the screening test as an indicator or rebuttable presumption.

31. The SAFRC member said that the screening test should not be determinative; an entity should be permitted to choose whether to perform the test and then should be permitted to choose whether to accept or to rebut the outcome of the test.
32. The AOSSG member said that AOSSG members had mixed views on the screening test. Some members preferred a mandatory and determinative screening test, other members suggested removing the screening test. One member recommended the Board undertake an effect analysis before finalising the amendments. Another member agreed with the Board's tentative decision to make the screening test optional.
33. The IASB staff clarified the following points:
 - (a) The purpose of the screening test is to make it easier, simpler and less costly for entities to determine whether what they have acquired is just a set of assets or a business. It would apply in some straightforward cases when there is little risk that the outcome could deprive users of financial statements of material information.
 - (b) If the screening test identifies an asset purchase, no further assessment is needed. The Board's discussions so far had not focussed on whether further assessment should be prohibited (rather than merely not required) in those cases. The discussion with ASAF members had highlighted concerns about whether such a prohibition would be appropriate and feasible.
 - (c) In some cases, the screening test might identify as an asset purchase a transaction that the full assessment would have identified as a business combination. For the following reasons, that outcome is unlikely to deprive users of financial statements of material information:
 - (i) 'Core goodwill' is economically present in the acquisition of a business combination but is not present in an asset purchase.² But, if substantially all the fair value of the gross assets acquired (including core goodwill) is concentrated in a single asset, not recognising the core goodwill seems acceptable on materiality grounds.

² Paragraphs BC313-BC318 of the Basis for Conclusions on IFRS 3 describe 'core goodwill'. As discussed there, because goodwill is measured as a residual, the carrying amount of goodwill also includes several other factors.

- (ii) There are some other accounting differences between an asset purchase and the acquisition of a business. They affect, for example, deferred tax, contingent consideration and acquisition costs. They reflect differences between particular accounting standards, not economic differences between an asset purchase and the acquisition of a business. Thus, for transactions within the proposed narrow scope of the screening test, classifying a transaction as an asset purchase is unlikely to result in a loss of material information.
 - (d) The screening test never identifies any transaction as the acquisition of a business. If the screening test does not identify an asset purchase, the entity must carry out a further assessment. And if the entity elected not to apply the screening test, it must carry out that same assessment.
 - (e) Making the screening test optional has some advantages:
 - (i) it reduces pressure on the detailed design of the test. Respondents raised a number of comments and questions about the design of the test;
 - (ii) it does not force entities to use the screening test in cases where they could reach the same answer more efficiently, and at less cost without using it;
 - (iii) it does not force entities to identify a transaction as an asset purchase if the entity has clearly acquired a business but the fair value of the assets acquired (including 'core' goodwill) is concentrated in one asset (or in a group of similar assets); and
 - (iv) by not being used as an indicator or as a rebuttable presumption, it does not force entities to apply both the screening test and the full assessment.
34. The FASB member noted that before finalising the amendments to its definition of a business the FASB had received feedback on the screening test similar to the feedback received by the Board. The FASB had considered changing the screening test to an indicator or to a rebuttable presumption; however, the FASB decided not to do that, because they would have complicated the guidance. The FASB did not consider making the screening test optional; however, he observed that the downside of an

optional screening test is that it is impossible to know whether an entity has performed the test.

35. The ANC member supported the Board's tentative decision to make the screening test optional, because it is simpler than an indicator or a rebuttable presumption.
36. The AcSB member appreciated the efforts made by the Board and the FASB to remain converged and noted that her analysis indicated those applying the different Standards should be able achieve converged outcomes. Her only concern was the fact that the two amendments that have different effective dates.

Goodwill and Impairment

37. ASAF members' advice was asked on the following possible approaches to improve the impairment testing of goodwill.
 - (a) *Goodwill accretion approach*—the EFRAG member sought feedback on an approach described in the EFRAG Discussion Paper *Goodwill Impairment Test: Can it be improved?* That approach aims to prevent a shielding effect that arises when goodwill is generated internally after a business combination.
 - (b) *Pre-acquisition Headroom (PH) approach*—this approach aims to prevent a shielding effect that arises from pre-acquisition headroom if goodwill is allocated to cash-generating units (CGUs) that the acquirer already held before the acquisition.
 - (c) *Single method*—using a single method, ie either value in use (VIU) or fair value less costs of disposal (FVLCD), as the sole basis for determining recoverable amount instead of the current requirement to use the higher of the two.

Goodwill accretion and the PH approach

38. ASAF members generally expressed concerns that both goodwill accretion and the PH approach would add complexity to the impairment testing model.
39. The FASB member highlighted that the amount of goodwill accretion is not calculated on a compound basis, making it inconsistent with its underlying assumption.

40. Some members (GLASS and FASB) stated that in their jurisdiction, information about goodwill and about goodwill impairment is viewed as noisy, arbitrary and artificial and as a lagging indicator only, that provides confirmatory evidence only.
41. The SAFRC member said that the goodwill accretion approach would not identify an impairment loss on goodwill unless the estimated future growth rate is less than the growth rate assumed at the date of the acquisition.
42. The OIC member noted that the goodwill accretion approach would identify impairment losses sooner. He also commented that goodwill is not the present value of excess future returns but a residual amount, and thus it should be amortised over some specific period, such as the payback period.
43. The CASC member stated that the goodwill accretion and PH approaches are too complicated. In particular, the goodwill accretion approach would further increase the subjectivity of the goodwill impairment model. She also expressed concerns about how to measure the impact on a decrease of the original goodwill in the CGU.
44. The AASB/NZASB member said that both approaches aim to remove a shielding effect and that this effect could arise for other assets, such as other indefinite-lived intangible assets. She also stated that the allocation of goodwill should be simplified and the impairment methodology needs to address deferred tax issues.
45. The AOSSG member noted that there are mixed views about both approaches among AOSSG members. Some AOSSG members argued that requiring additional disclosure would be a better solution than making the impairment test more complex. They stated that an impairment loss on goodwill could be caused by the headroom already within an existing CGU(s) of the acquirer, not by the acquisition. Therefore, they thought the impairment loss should be allocated proportionally between the pre-acquisition headroom and goodwill, not fully to goodwill relating to the acquisition.
46. The ASBJ member stated that even though the ASBJ agrees with the basic assumption underlying the goodwill accretion approach (ie not to recognise internally generated goodwill), this approach is difficult to understand and use. Moreover, the PH approach would not be appropriate in terms of the objective of financial reporting in the *Conceptual Framework*.
47. The AcSB member stated that even though the goodwill accretion approach might not be complex to implement, it would be difficult for preparers to understand intuitively.

In addition, accreting an item artificially would conflict with standards setters' efforts to reduce the complexity of the standards.

Single method

48. The CASC member stated that FVLCD and VIU measurements would not produce significantly different measurements in most cases. However, if a single method is introduced for all other assets within the scope of IAS 36 *Impairment of Assets*, that would be a significant change.
49. The AASB/NZASB member thought that fair value methodology of discounted cash flows needs to be used as the sole basis for determining recoverable amount, with different assumptions permitted depending on the use of the asset. This would remove the arbitrary distinction that currently excludes from value in use the effect future enhancements and restructuring.
50. The SAFRC member commented that in some situations VIU differs significantly from FVLCD. For example, in the mining industry VIU, as described in IAS 36, is much less than FVLCD. If that VIU becomes the sole basis for determining recoverable amount, there will be significant impairment losses in that industry. The AASB/NZASB member agreed.
51. The OIC member supported using FVLCD or VIU depending on how an entity expects to recover the assets, in the light of its business model.

Project updates and agenda planning

52. The IASB staff presented an update on the IASB technical projects and a summary of how the Board had used the ASAF advice from the previous meeting.
53. The IASB staff noted that ASAF members had raised questions regarding the proposed agenda topics for the December 2017 ASAF meeting. In response the staff proposed to review the proposed topics and circulate an agenda for consideration by members.