

Effects Analysis process—moving forward

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Objectives of this session

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We are seeking the advice of the IFRS Advisory Council members on any potential changes in our Effects Analysis process

Why now?

Recent publication of comprehensive Effects Analysis for new IFRS Standards reflecting the recommendations raised in 2014 by an international working group

Ongoing discussion among standard-setters, regulators and academics about the role of Effects Analyses within the standard-setting process

Forthcoming review of our Due Process Handbook



Opportunity to review if:

- the existing Effects Analysis process is appropriate to achieve our objectives; and
- such objectives could be achieved in a more effective way



Opportunity to incorporate any changes in our Due Process Handbook

Today's agenda

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- Background
 - Introduction
 - History
- Existing process
 - Due Process Handbook
 - Recommendations from Effects Analysis Consultative Group
- Recent experience
- Questions for the break-out discussion
 - Overall question
 - Detailed questions



Background

Introduction and history

What is an Effects Analysis?

- A process for assessing the likely effects of an IFRS Standard, which is undertaken as new requirements are developed

What are the objectives of an Effects Analysis?

- Strengthen the standard-setting process by enhancing its transparency and accountability
- Provide evidence to make decisions (eg whether new accounting requirements should be finalised)

Who are the users of an Effects Analysis?

- Those interested in the Board's work

History

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2007

The requirement for an analysis of the effects of a new IFRS Standard or a major amendment is included in the Due Process Handbook

2008

The Board publishes its first separate Effects Analysis which accompanies IFRS 3 *Business Combinations*

2012-2013

The report of the Trustees' Strategy Review 2011 asks to further clarify the role of the Effect Analysis in the Board's due process; an Effects Analysis Consultative Group is formed

2014

The Effects Analysis Consultative Group completes its work by issuing a report with some recommendations for the Board

2016-2017

The recommendations of the Effects Analysis Consultative Group are adopted in the Effects Analyses for IFRS 16 *Leases* and IFRS 17 *Insurance Contracts*



Existing process

Due Process Handbook (paragraphs 3.73-3.76)

- The Board should assess the

1 likely costs of implementing new requirements

2 likely ongoing associated costs and benefits

(the costs and benefits are collectively referred to as effects)

in the light of its objective of financial reporting transparency

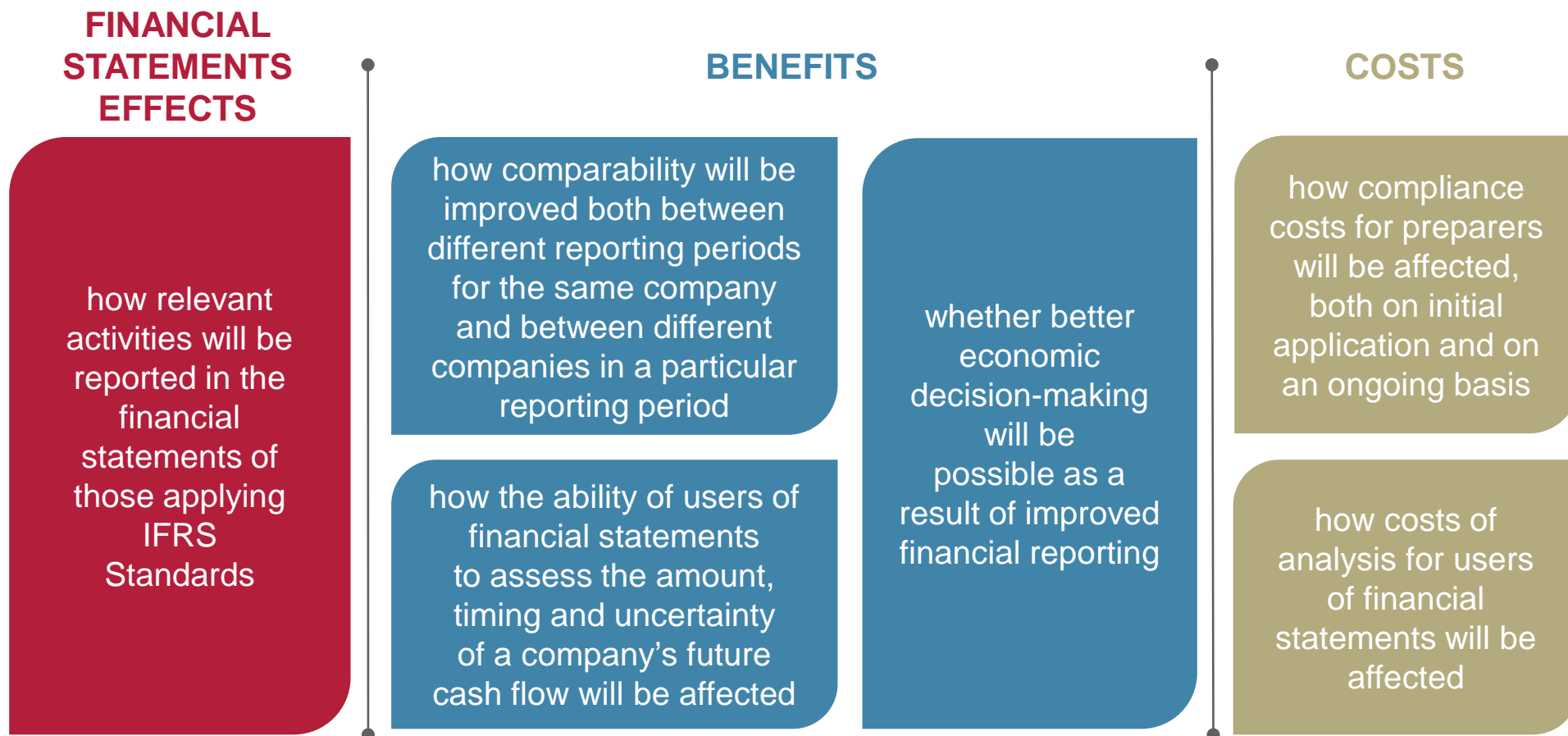
in comparison to the existing financial reporting requirements

throughout the development of a new or amended Standard

The analysis is not expected to include a formal quantitative assessment of the overall effect of a Standard. Initial and ongoing costs and benefits are likely to affect different parties in different ways.

- The Board
 - gains insight on the likely effects through its
 - formal exposure of proposals
 - fieldwork, analysis and consultations with relevant parties through outreach
 - presents the likely effects as part of, or with, the Basis for Conclusions on each Exposure Draft and Standard
- The level of analysis is tailored to the type of changes, with more analysis undertaken for new Standards and major amendments

- Examples of issues to consider in an Effects Analysis





Existing process

Recommendations from
Effects Analysis Consultative Group

Effects Analysis Consultative Group

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- Effects Analysis Consultative Group (EACG)¹
 - working group formed in 2013 following the Trustees' Strategy Review 2011
 - composed of international stakeholders (15 members + IOSCO and European Commission as observers)
 - had the goal of developing an agreed methodology for field testing and effects analyses

EACG completed its work in November 2014 by issuing a report with some recommendations for the Board

¹ See the [Effects Analysis Consultative Group page](#) on IFRS Foundation website for further information

EACG recommendations

1. *Focus of Effects Analysis*

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DO

How changes are likely to affect the quality of financial information for the purposes of making decisions about evaluating a company's management or about providing resources to the company

How those changes are likely to affect general purpose financial reports

Why those changes will improve the quality of general purpose financial reports

Why those changes are justifiable for the Board that should assess the likely effects on the direct costs to preparers and users of financial statements

DON'T

The Board is not required to assess any possible broader economic consequences, because these are beyond its objective

EACG recommendations

2. *Financial stability*

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DO

As a member of the Financial Stability Board (FSB), the Board is committed to pursue the maintenance of financial stability, maintain the openness and transparency of the financial sector and implement IFRS Standards

The Board should focus on ensuring that investors have high quality, transparent and comparable information

The Board should continue to engage with the FSB to ensure that the FSB is aware of proposed changes to financial reporting and that the FSB has sufficient time to assess and address how changed financial reporting information should be incorporated into the FSB's own monitoring systems

DON'T

The Board should not tailor financial reporting to meet the needs of other parties that use general purpose financial statements for their own objectives—including determining taxable income, determining distributable reserves, statistical purposes and regulation

The format of the analysis of the likely effects of a proposed change in financial reporting should reflect the stage of the proposals

Research stage

An analysis of the perceived deficiencies and the possible solutions are an integral part of the discussion or research paper

Exposure Draft stage

The Basis for Conclusions should set out why the Board is proposing a particular change to financial reporting requirements, including referring to the evidence it has collected or the outreach it has undertaken

IFRS Standard

The Board should generally prepare a separate Effects Analysis Report which

- is well-focused
- summarises the likely effects and how the Board made the assessments
- is included with the package of documents balloted by the Board



Recent experience

New IFRS Standards and major amendments

Recent experience

Timing and format

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	Discussion Paper	Exposure Draft	IFRS Standard
IFRS 16 Leases (January 2016)	Discussion of deficiencies and possible solutions	Analysis of costs and benefits included in the Basis for Conclusions	Separate Effects Analysis Report ¹
Amendments to IFRS 4 Insurance Contracts (September 2016)	n.a.	Discussion of stakeholders' concerns and possible solutions	Analysis of costs and benefits included in the Basis for Conclusions ²
IFRS 17 Insurance Contracts (May 2017)	Discussion of deficiencies and possible solutions	Brief analysis of costs and benefits included in the Basis for Conclusions	Separate Effects Analysis Report ³

1 [Effects Analysis on IFRS 16](#) available on IFRS Foundation website

2 Paragraphs BC283-BC299 of the Basis for Conclusions on IFRS 4—Effects analysis of Applying IFRS 9 with IFRS 4

3 [Effects Analysis on IFRS 17](#) available on IFRS Foundation website

Recent experience

Content at different stages

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	Discussion Paper	Exposure Draft	IFRS Standard
1 Qualitative analysis of deficiencies	✓	✓	✓
2 Case studies illustrating deficiencies	✗	✗	✓
3 Qualitative analysis of the costs of the proposed solutions	✗	✓	✓
4 Qualitative, and where possible quantitative, analysis of benefits	✗	✓	✓
5 Comparison of existing requirements vs proposed / new requirements	✗	✓	✓

Recent experience

Content of final document

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Topics mentioned in Due Process Handbook

Benefits (quality of information and comparability)

Costs for preparers and users of financial statements

Effects on a company's financial statements

Additional topics

Other effects

Overview of new requirements

Companies affected

Illustrations

Differences between IFRS Standard and US GAAP

	IFRS 16 <i>Leases</i>	IFRS 17 <i>Insurance Contracts</i>	Amendments to IFRS 4 <i>Insurance Contracts</i>
Benefits (quality of information and comparability)	✓	✓	✓
Costs for preparers and users of financial statements	✓	✓	✓
Effects on a company's financial statements	✓	✓	✓
Other effects	✓ ¹	✓ ¹	✗
Overview of new requirements	✓	✓	✗
Companies affected	✓	✓	✗
Illustrations	✓	✓	✗
Differences between IFRS Standard and US GAAP	✓	✓ ²	✗

¹ Refer to examples in slides 20-21

² High-level comparison only

Recent experience

Content—example of other effects

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- In the final Effects Analysis for IFRS 16 and IFRS 17 the Board considered effects beyond costs and benefits—effects that are specific to the changes introduced and that therefore vary by project
- For example, the Board considered
 - the likely effect of IFRS 16 on the cost of borrowing, given the expected increase in leverage due to recording of liabilities that were previously off balance sheet¹
 - the interaction between IFRS 17 and regulatory frameworks, given that in some cases there are similarities between accounting and regulatory requirements for insurance companies²

¹ See Section 7.1 of the [Effects Analysis on IFRS 16](#)

² See Section 7.2 of the [Effects Analysis on IFRS 17](#)

- The primary goal of the Board is to improve general purpose reporting of a company's activities in a cost-beneficial way, rather than to assess any wider potential consequences of changes to reporting requirements
- Nonetheless, IFRS 16 and IFRS 17 effects analyses indirectly considered some wider economic effects
- For example, the Board provided a qualitative analysis of
 - whether IFRS 16 might give rise to behavioural changes that would affect the leasing market¹
 - how the improved transparency resulting from IFRS 17 would contribute to long-term financial stability²

¹ See Section 7.4 of the [Effects Analysis on IFRS 16](#)

² See Section 4.2 of the [Effects Analysis on IFRS 17](#)

- The Board's evaluation of costs and benefits is mainly qualitative, rather than quantitative
- Costs
 - Quantifying the costs involved in implementing new accounting requirements depends on specific circumstances and other improvements that are made at the time of implementation
- Benefits
 - The analysis mainly considers the benefits of better economic decision-making that result from improved financial reporting
 - In some cases, the assessment of effects can be supported with quantitative data, such as data available in the financial statements of companies (see slide 23)

Recent experience

Methodology—effects on financial statements

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IFRS 16

- The Board undertook quantitative analysis to compare (i) the likely effects on the leverage of companies of bringing many operating leases onto balance sheets with (ii) how investors and analysts adjust reported leverage to consider the effect of off balance sheet leases
- That quantitative analysis supported the qualitative analysis of the benefits of the change in lease accounting
- The Board used information about operating leases disclosed in the notes to the financial statements

IFRS 17¹

A quantitative analysis was not useful nor possible because

- insurers will implement IFRS 17 requirements from many different perspectives—the existing insurance contracts Standard, IFRS 4, is an interim Standard that essentially grandfathered national GAAP
- it is not possible, using the information disclosed in the notes to the financial statements, to determine the amounts by which insurance liabilities determined under one national GAAP would need to be adjusted to be compliant with IFRS 17 requirements

¹ The Effects Analysis on IFRS 17 focuses on explaining that changes in a company's financial statements introduced by IFRS 17 will vary by company and by jurisdiction, depending on practices applied today



Questions for the break-out discussion

Overall question and detailed questions

Overall question

How can we improve the effectiveness of our Effects Analyses?

Some factors to consider when discussing the detailed questions on the following pages

- Our mission statement—bring transparency, accountability and efficiency to financial markets around the world by developing IFRS Standards
- Feasibility of the analysis, in the light of:
 - techniques available
 - resources and time available
 - required engagement from third parties
- Differences between jurisdictions (eg different starting points for accounting requirements, different business practices and environment)

Detailed question 1—scope

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Q

1

What do you think the scope¹ of an Effects Analysis should be? Why?

Example of aspects to consider

- Which standard-setting projects should be subject to an Effects Analysis
- Which projects should the Board prioritise
- For narrow-scope amendments to IFRS Standards, would the benefits of performing an Effects Analysis outweigh the costs

¹ Refer to slides 8-9 for the requirements in the Due Process Handbook

Detailed question 2—timing

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Q

2

What do you think the timing¹ of our Effects Analyses should be? Why?

Example of aspects to consider

- At which stages an Effects Analysis should be initiated
- Ongoing process throughout the standard-setting process or mainly at final stage
- Timeliness of the analysis before final stage
- Difficulties of engaging with stakeholders early in the process to test the effects of draft requirements

¹ Refer to slides 17-18 for recent experience

Detailed question 3—content

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Q

3

What do you think the content¹ of our Effects Analyses should be? Why?

Example of aspects to consider

- Content of the Effects Analysis at different stages of the standard-setting process; aspects that the Board should prioritise
- Focus on costs and benefits or extension to wider economic effects (eg effects on financial stability and on possible behavioural changes)
- Responsibility to assess macro-economic effects (eg effects of unemployment rates)

¹ Refer to slides 19-21 for recent experience

Detailed question 4—methodology

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Q

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What methodology¹ do you think we should use for assessing the effects? Why?

Example of aspects to consider

- Qualitative or quantitative evaluation of effects
- Variation of effects by companies and by jurisdictions
- How to quantify of (i) costs (ii) benefits and (iii) effects in the financial statements in a reliable manner
- Difficulties to isolate wider economic effects resulting from changes in IFRS Standards from other factors

¹ Refer to slides 21-23 for recent experience

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