STAFF PAPER

November 2019

## IFRS® Interpretations Committee meeting

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| **Project** | **2020 Agenda Consultation** |
| Paper topic | Approach to the Request for Information |

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## Introduction

1. In Agenda Paper 2A we have set out the Board's approach to the 2020 Agenda Consultation. That consultation will include a Request for Information (RFI) which will be published in September 2020. The RFI will include a description of potential projects for the Board's future work plan for comment by stakeholders.

2. The objective of this session is for Committee members to help us identify and develop a description of those potential projects. We are not seeking a consensus view from the group.

3. In Appendix A to this paper we have noted the topics suggested by members for discussion today. Where members have provided suggested solutions or an indication of size we have included this information.

4. We have not prepared any assessment or added an analysis of the topics suggested; this is a fact-finding session. We have, however, tried to categorise the topics suggested by theme to give structure to the discussions.

## Proposed approach to the discussions

5. We suggest the following approach to the discussions:

   (a) Discussion of suggestions for potential new topics to add to the work plan described in the appendix—including members reactions to topics; and

(b) Discussion of the financial reporting environment and other comments received, such as overall balance of the Board’s activities and comments on the agenda consultation process.

## Appendix Suggested topics

This appendix consists of:

a) potential new topics to add to the work plan–for discussion;

b) suggestions relating to existing or planned projects;

c) considerations for planned post-implementation reviews;

d) comments received on the balance of the Board's activities.

Where possible, we have retained the wording used by Committee members to describe each of the issues. Some suggestions have been summarised to aid discussion.

| **Potential new topics to add to the work plan–for discussion** |
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| ***1 On the theme of intangibles:*** |
| IAS 38 is an old standard which is inconsistent on several subjects such as intellectual property licensing acquired–IAS 38 deals with the right to use a licence, but not the right to receive access to a licence, notably on the cloud. It is also inconsistent with IFRS 15 where this distinction does exist for IP licenses sold. There is a long-standing inconsistency in accounting between the separate acquisition of intangibles (IAS 38) and intangibles acquired in a business combination (IFRS 3). Should cover all intangibles, whether assets or working capital, eg advance payment within a service contract. Should lead to a reduction in recognised (capitalised) intangibles. |
| With the technological changes that are happening in a variety of industries, this Standard is used more and more often. We've referred to it in our discussions on: crypto currency, software scoped out of leases, software in the cloud, etc. In the automotive and transportation industry, emissions trading schemes (that are increasingly coming into effect globally) all seem to end up in IAS 38 and, in nearly all cases that we have personally encountered, IAS 38 is deficient in providing any framework and/or guidance on how to account for these different topics. Affects most entities given the prevalence of technology developments. Would be a large project to rewrite IAS 38. |
| IAS 38 has been overtaken by changing economic and technological environments. As these assets become more complex and diverse, the Standard is increasingly challenged. IAS 38 often functions as a residual standard. Recognition and measurement may not always reflect the economic characteristics or complexity of contractual arrangements. Need to address scope (eg crypto assets; software as service arrangements; interaction with IFRS 16 lessees). Definition of control may no longer be appropriate eg whether run on own servers or hosted. Variable payments may also make initial cost difficult to establish. Thought needs to be given to subsequent measurement eg is FV through P&L appropriate? A large project. |
| Consider how better information about intangible assets could be provided through financial reporting as part of the Board's work on Better Communications. |
| Intangibles are a major factor in driving value creation in the current global economy. Due to the age of IAS 38 there are concerns about adequacy when identifying, recognising and measuring internally generated assets. Important interrelationship with IAS 36. Increased use of digital/ cryptocurrency assets. Intangibles need as stable a platform as tangible assets. Given the rate of change in technology this topic will become increasingly relevant. |
| ***2 Relating to crypto currencies, commodities and other investments:*** |
| **Crypto currencies:** Accounting for crypto currencies may not be clear, based on current standards, and the application of those standards may not give the most relevant information. Need a framework. They have various features and can be held in different forms. The Agenda Decision focused on a relatively narrow definition and only considered direct holdings. Consider Libra and similar instruments as well as indirect holdings. Also the definition of cash in IAS 32–is that fit for purpose? Is it appropriate to consider all assets that are not tangible and do not fit into a specific standard as intangibles? Although direct holdings are not |

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| yet material or pervasive, the market is moving rapidly. A new Standard may be necessary as IAS 38 is a 'residual' standard. Likely to be medium size. |
| **Crypto currencies:** Addressed by IFRIC, but uncertain whether the application of IAS 38 faithfully depicts the economic substance. Agenda Decision did not address other areas of cryptocurrencies such as ICOs. Area is expected to grow fast. Would be a large project. |
| **Crypto currencies:** This will be a large issue for reporters in the near future. Given the time taken to address issues, this is the right time to address it. At the moment, the impact is small but they are becoming more prevalent. Also believes the current IFRIC Agenda Decision on the issue results in a nonsensical answer that would not lead to high quality financial reporting. This would be a medium project. |
| **Other investments:** Investments of a non-financial nature, including commodities (gold, precious metals and cryptocurrencies), artefacts and antiques, etc. This type of investment has become popular, but its accounting is not addressed in IFRS Standards. It affects a wide range of stakeholders, regulators, issuers and investors. A medium project to perform standard-setting for a wide array of other investments. |
| ***3 Other suggested topics:*** |
| **Cash flows:** Presentation in cash flows shows divergent practice. Different issues raised with IFRIC. The proposed amendments to IFRS 7 in PFS may not be sufficient. Needs of users would be an important input. |
| **Discount rates**: Difficult to convey to investors and others the purpose of so many different rates used in Standards to discount liabilities. Also question the different recognition thresholds for various liabilities eg IAS 7 vs IFRS 9. Significantly reducing the number of discount rates would simplify and enhance understandability. Consider whether a single rate–such as the incremental rate the entity pays on borrowings–could be used for the initial recognition of all liabilities. Consider whether/ when this is adjusted for subsequent remeasurement. There may need to be some exceptions, eg IAS 12. |
| **Going concern:** Disclosures relating to going concern (including 'close calls') warrant proper consideration within IFRS Standards, building on the IFRIC agenda decision in July 2014. Question whether paragraph 122 in IAS 1 (referred to in the IFRIC agenda decision) is an adequate technical reference given that disclosure of judgements regarding the going concern assessment would not have an effect on the amounts recognised in the financial statements.<br>More generally, entities' disclosures under IAS 1.122 and IAS 1.125 often appear boiler-plate. Developments to date under the Disclosure Initiative have not focused on improving these requirements and IAS 1 is not in the scope of the pending project Disclosure Initiative - Targeted Standards-level Review of Disclosures. Preparers are confused about the purpose of these disclosures and how they interact with disclosure requirements in other standards. This could be a small project, perhaps under the umbrella of Better Communication. |
| **High and hyperinflation:** IAS 29 is old and lacks relevant use in practice for several years. High and hyperinflation is now re-emerging, especially in South America, eg Argentina, Venezuela. Quantitative easing programmes can also lead to high inflation. The current scope threshold is too high. Lack of an appropriate treatment means many numbers in the balance sheet, such as fixed assets at cost, are irrelevant and wrong. Overhaul IAS 29 or develop a new Standard re high inflation. A large project. |
| **Interim reporting:** IAS 34 focuses on whether information is new since the last *annual* reporting period and this can lead to repetitive disclosures in Q1, Q2, etc. in the years when a new IFRS, such as IFRS 16, is first applied. |
| **Pensions:** Amend IAS 19 to clarify the definition of past service cost and gains and losses on settlement. Debates arising from this concern: the impact of guaranteed minimum payment equalisation in the UK, as either a past service cost or a remeasurement; accounting for buy-in, buy-out, and wind up; accounting for the impact on benefits deriving from a change in law, with no change to the deeds or rules of a defined benefit plan. |

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| **Separate financial statements:** IAS 27 does not provide enough information on separate financial statements even though their main purpose is different from that of consolidated financial statements. Separate financial statements are very important in some jurisdictions because they are required by law. May also provide additional information to users. Affects investors, lenders, creditors, regulators and tax authorities. Overhaul IAS 27: a small or medium project–consider help from jurisdictions, eg Korea. |
| **SMEs:** The IFRS for SMEs was designed to provide an easier framework for non-publicly accountable entities. The Board currently seems to favour making this IFRS-lite. That framework aids many medium entities (and possibly subsidiaries of larger entities), but does not address the millions of micro-entities in developing markets who don't have a framework to use. This framework would be a feeder for companies eventually moving to SMEs or even full IFRS. This would be a medium project in conjunction with jurisdictions who have already developed such a framework. It would have a big impact in developing economies. |
| **Tax:** Differences between the tax-base value of assets and liabilities and their carrying values gives rise to temporary differences. Although the balance sheet approach makes sense conceptually, it has proved difficult to apply practically alongside the transition to IFRS 16. The ED *Deferred Tax Assets and Liabilities Arising from a Single Transaction* does not improve clarity. Revise IAS 12 to suppress the balance sheet approach. Create a new concept based on income tax flows, reconciling the tax and accounting bases, and align the concept with the income tax practice of the company. |
| **Suggestions relating to existing or planned projects** |
| **Discontinued operations IFRS 5:** A number of IFRIC submissions on IFRS 5 are unresolved. One of the 2015 Agenda Consultation goals was a PIR of IFRS 5. Not yet started. Issues continue to arise in practice. Concerns about lack of clear guidance and diversity in application. May warrant a fundamental review of the Standard. |
| ***Some comments on the equity method research project:*** |
| (a) The cost of investments has given rise to queries with IFRIC: investment in a subsidiary in a step acquisition; determining the cost of a subsidiary when IFRS 9 applied previously; or cost of an associate or JV applying the equity method. Applying the equity method is often used in the reporting by subsidiaries, but this has legal and tax implications. Need to overhaul IAS 28 and IAS 27. (Extensive expertise in Brazil.) |
| (b) IAS 28 seems to be incomplete. It is a mixture of a measurement concept and a one-line consolidation. Also 'significant influence' is not clearly defined. A large topic, but many jurisdictions have experience and could help, including Korea (paper Oct 2014). Associates and JVs are often material; current accounting may mislead investors. |
| (c) We have identified numerous issues with equity accounting over the past years. This project would be far reaching and impact reporters globally. This would be a large project. |
| (d) There has been much debate about whether the equity method is primarily a method of consolidation or a valuation method. IAS 28 notes that many procedures appropriate for the application of the equity method are similar to consolidation procedures described in IFRS 10. IAS 28 also explains that concepts underlying the acquisition of a subsidiary are also adopted in accounting for the acquisition of an associate or joint venture. However, it is unclear what those concepts are as no further explanation is given. As there is no clear principle underlying the application of the equity method (consolidation or valuation), different views have arisen on how to account for certain transactions, for example–in piecemeal acquisition; contributions of non-monetary assets; equity transactions in the associate's own financial statements. This would be a large project. |
| (e) Increase the priority of the existing project on equity accounting. |
| (f) There is one specific topic that was discussed by the IFRIC on how an entity accounts for the acquisition of an interest in an associate or joint venture from an entity under common control. There were diverging, albeit minority views, on the applicability of IAS 28 in dealing with this. If outside the BCUCC project this may not be addressed. May be a small subset of issuers, but provides the potential for structuring and inconsistent reporting for economically similar transactions. |

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| **Fair value disclosures:** IFRS 13 reconciliation requirements could be considered to be prescriptive. It would be helpful if they were more along the lines of IFRS 7 expected credit loss disclosures where it is the objective/nature of what needs to be understood that is required by the Standard, rather than dictating line items. Also, IFRS 13 *requires* extensive disclosures for interims, unlike most other standards. This is perceived as disproportionate. (See also new topic above on 'interim reporting'.) |
| **Onerous contracts:** How should 'benefits' be analysed and considered when determining if a contract is onerous? This has been discussed by the Board as part of the ED and will be taken up as part of IAS 37 project. |
| **Pensions:** Increase priority of existing project on pensions that depend on asset returns. |
| **PIRs:** Focus on post-implementation reviews already identified, such as PIR of IFRS 5 and IFRS 10-12, as robust PIRs are important to the overall development of financial reporting. |
| **Risk sharing**: We have seen an increase in risk sharing arrangements, sometimes called collaboration arrangements, especially in pharma, tech and aerospace & defence. Difficult to account for as they do not fit with IFRS 11. Based on sharing risk, rather than control. May overlap with joint operations. [*Staff note*: likely to be addressed by PIR of IFRS 11.] |
| **Variable consideration:** Focus on topics already identified, such as variable and contingent consideration, to make effective improvements on a timely basis. |
| **Variable consideration:** In service concessions, variable payments to the grantor can be made over the contract life (> 10 years) and are adjusted annually for inflation. Treating such variable payments as an expense creates a mismatch between expenses and related revenues. The short-term effect can also postpone dividends. Treat as an amortised asset, similar to IFRS 16. IFRIC has discussed some possible wording that could be used to amend IFRIC 12, IAS 38, IAS 16 and possibly IFRS 3. |
| **Considerations for planned post-implementation reviews** |
| **IFRS 9:** Long term securities measured at FV going through P&L or FV through OCI are not considered appropriate categories when held by an industrial entity because the sale is not reported as part of its financial performance. Suggestion is to suppress such use of FV through OCI, not reclassified subsequently to P&L, and create a category 'FV through OCI reclassified to P&L'. Reinstate provisions using the impairment test for this new category. |
| **IFRS 9:** As IFRS 9 is implemented by entities, divergent practices may emerge. This could be significant. IFRS 9 is principle-based and it is important those principles are understood and implemented consistently so regulators and markets have confidence in the resulting expected credit loss numbers. Not proposing bringing the PIR forward, but carrying out implementation work that could feed into a future PIR. Enable practice issues to be highlighted and dealt with rapidly. Board could start collecting information for PIR or targeted action, ie active monitoring and information gathering, in addition to IFRIC addressing questions raised. Likely to be medium in size. |
| **IFRS 9:** Contractually-linked instruments should either be taken to IFRIC or covered by the IFRS 9 PIR |
| **Comments received on the balance of the Board's activities** |
| Standards are difficult to apply operationally. Need PIRs to ensure that conceptual accounting is applied practically and the results are reflective of the economics and structure of each particular transaction. |
| Should continue with enhanced focus on consistent application and maintenance. |
| Set the agenda in a way that allows sufficient capacity to address urgent new matters–that will inevitably arise–in a timely manner, especially in the light of IFRSs 9,15,16. |
| In adding new topics, consider the balance between the significant resources needed and the improvement it would make to financial reporting. For example, on FICE the Board took an approach that addresses known practice issues, rather than investing substantial resources developing new principles. Support this approach. Consider whether limited resources should instead be used to fix |

known and widespread practice issues known for some time, eg mandatory purchases of NCIs or variable consideration.