

IFRIC Update—June 2019

IFRIC *Update* is a summary of the decisions reached by the IFRS Interpretations Committee (Committee) in its public meetings.

The Committee met in London on **11-12 June 2019**, and discussed:

Committee's tentative agenda decisions

- [Fair Value Hedge of Foreign Currency Risk on Non-Financial Assets \(IFRS 9 *Financial Instruments*\)—Agenda Paper 4](#)
- [Compensation for Delays or Cancellations \(IFRS 15 *Revenue from Contracts with Customers*\)—Agenda Paper 8](#)
- [Lessee's Incremental Borrowing Rate \(IFRS 16 *Leases*\)—Agenda Paper 2](#)
- [Lease Term and Useful Life of Leasehold Improvements \(IFRS 16 *Leases* and IAS 16 *Property, Plant and Equipment*\)—Agenda Paper 3](#)
- [Presentation of Liabilities or Assets Related to Uncertain Tax Treatments \(IAS 1 *Presentation of Financial Statements*\)—Agenda Paper 7](#)
- [Disclosure of Changes in Liabilities Arising from Financing Activities \(IAS 7 *Statement of Cash Flows*\)—Agenda Papers 5–5A](#)
- [Subsequent Expenditure on Biological Assets \(IAS 41 *Agriculture*\)—Agenda Paper 9](#)

Committee's agenda decisions

- [Holdings of Cryptocurrencies—Agenda Paper 12](#)
- [Costs to Fulfil a Contract \(IFRS 15 *Revenue from Contracts with Customers*\)—Agenda Paper 10](#)
- [Subsurface Rights \(IFRS 16 *Leases*\)—Agenda Paper 11](#)
- [Effect of a Potential Discount on Plan Classification \(IAS 19 *Employee Benefits*\)—Agenda Paper 13](#)

Items on the current agenda

- [Sale of a Single Asset Entity Containing Real Estate \(IFRS 10 *Consolidated Financial Statements*\)—Agenda Paper 6](#)
- [Lack of Exchangeability \(IAS 21 *Effects of Changes in Foreign Exchange Rates*\)—Agenda Papers 14–14C](#)

Other matters

- [Matters Reported to the Board—Agenda Paper 15](#)
- [Committee Work in Progress—Agenda Paper 16](#)

Related information

Next scheduled IFRS Interpretations Committee meeting:

- 16-17 September 2019

Interpretations Committee open items

For further information about IFRS Interpretations Committee activities including how to receive IFRIC Updates follow the [Interpretations Committee group page](#).

Committee's tentative agenda decisions

The Committee discussed the following matters and tentatively decided not to add them to its standard-setting agenda. The Committee will reconsider these tentative decisions, including the reasons for not adding the matters to its standard-setting agenda, at a future meeting. The Committee invites comments on its tentative agenda decisions. Interested parties may submit comments on the [open for comment](#) page by 20 August 2019. All comments will be on the public record and posted on our website unless a responder requests confidentiality and we grant that request. We do not normally grant such requests unless they are supported by good reason, for example, commercial confidence. The Committee will consider all comments received in writing by 20 August 2019; agenda papers analysing comments received will include analysis only of comments received by that date.

Fair Value Hedge of Foreign Currency Risk on Non-Financial Assets (IFRS 9 Financial Instruments)—Agenda Paper 4

The Committee received two requests about fair value hedge accounting applying IFRS 9. Both requests asked whether foreign currency risk can be a separately identifiable and reliably measurable risk component of a non-financial asset held for consumption that an entity can designate as the hedged item in a fair value hedge accounting relationship.

Hedge accounting requirements in IFRS 9

The objective of hedge accounting is to represent, in the financial statements, the effect of an entity's risk management activities that use financial instruments to manage exposures arising from particular risks that could affect profit or loss (or other comprehensive income) (paragraph 6.1.1 of IFRS 9).

If all the qualifying criteria specified in IFRS 9 are met, an entity may choose to designate a hedging relationship between a hedging instrument and a hedged item. One type of hedge accounting relationship is a fair value hedge, in which an entity hedges the exposure to changes in fair value of a hedged item that is attributable to a particular risk and could affect profit or loss.

An entity may designate an item in its entirety, or a component of an item, as a hedged item. A risk component may be designated as the hedged item if, based on an assessment within the context of the particular market structure, that risk component is separately identifiable and reliably measurable.

In considering the request, the Committee assessed the following:

Can an entity have exposure to foreign currency risk on a non-financial asset held for consumption that could affect profit or loss?

Paragraph 6.5.2(a) of IFRS 9 describes a fair value hedge as 'a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or a component of any such item, that is attributable to a particular risk and could affect profit or loss'.

Therefore, in the context of a fair value hedge, foreign currency risk arises when changes in exchange rates result in changes in the fair value of the underlying item that could affect profit or loss.

Depending on the particular facts and circumstances, a non-financial asset might be priced—and its fair value determined—only in one particular currency at a global level and that currency is not the entity's functional currency. If the fair value of a non-financial asset is determined in a foreign

currency, applying IAS 21 *The Effects of Changes in Foreign Exchange Rates* the measure of fair value that could affect profit or loss is the fair value translated into an entity's functional currency (translated fair value). The translated fair value of such a non-financial asset would change as a result of changes in the applicable exchange rate in a given period, even if the fair value (determined in the foreign currency) were to remain constant. The Committee therefore observed that in such circumstances an entity is exposed to foreign currency risk.

IFRS 9 does not require changes in fair value to be expected to affect profit or loss but, rather, that those changes could affect profit or loss. The Committee observed that changes in fair value of a non-financial asset held for consumption could affect profit or loss if, for example, the entity were to sell the asset before the end of the asset's economic life.

Consequently, the Committee concluded that, depending on the particular facts and circumstances, it is possible for an entity to have exposure to foreign currency risk on a non-financial asset held for consumption that could affect profit or loss. This would be the case when, at a global level, the fair value of a non-financial asset is determined only in one particular currency and that currency is not the entity's functional currency.

If an entity has exposure to foreign currency risk on a non-financial asset, is it a separately identifiable and reliably measurable risk component?

Paragraph 6.3.7 of IFRS 9 permits an entity to designate a risk component of an item as the hedged item if, 'based on an assessment within the context of the particular market structure, the risk component is separately identifiable and reliably measurable'.

Paragraph 82 of IAS 39 *Financial Instruments: Recognition and Measurement* permits the designation of non-financial items as hedged items only for foreign currency risks, or in their entirety for all risks, 'because of the difficulty of isolating and measuring the appropriate portion of the cash flows or fair value changes attributable to specific risks other than foreign currency risks'. Paragraph BC6.176 of IFRS 9 indicates that, in developing the hedge accounting requirements in IFRS 9, the Board did not change its view that there are situations in which foreign currency risk can be separately identified and reliably measured. That paragraph states that the Board 'learned from its outreach activities that there are circumstances in which entities are able to identify and measure many risk components (not only foreign currency risk) of non-financial items with sufficient reliability'.

Consequently, the Committee concluded that foreign currency risk can be a separately identifiable and reliably measurable risk component of a non-financial asset. Whether that is the case will depend on an assessment of the particular facts and circumstances within the context of the particular market structure.

The Committee observed that foreign currency risk is separately identifiable and reliably measurable when the risk being hedged relates to changes in fair value arising from translation into an entity's functional currency of fair value that, based on an assessment within the context of the particular market structure, is determined globally only in one particular currency and that currency is not the entity's functional currency. The Committee noted, however, that the fact that market transactions are commonly settled in a particular currency does not necessarily mean that this is the currency in which the non-financial asset is priced—and thus the currency in which its fair value is determined.

Can the designation of foreign currency risk on a non-financial asset held for consumption be consistent with an entity's risk management activities?

Paragraph 6.4.1(b) of IFRS 9 requires that, at the inception of a hedging relationship, 'there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge'. Accordingly, the Committee observed that, applying IFRS 9, an entity can apply hedge accounting only if it is consistent with the entity's risk management objective and strategy for managing its exposure. An entity therefore cannot apply hedge accounting solely on the basis that it identifies items in its statement of financial position that are measured differently but are subject to the same type of risk.

To the extent that an entity intends to consume a non-financial asset (rather than to sell it), the Committee observed that changes in the fair value of the non-financial asset may be of limited significance to the entity. In such cases, an entity may not be managing or hedging risk exposures on the non-financial asset and, in that case, it cannot apply hedge accounting.

Other considerations

An entity applies all other applicable requirements in IFRS 9 in determining whether it can apply fair value hedge accounting in its particular circumstances, including requirements related to the designation of hedging instruments and hedge effectiveness. For example, an entity would consider how its hedge accounting designation addresses any differences in the size, depreciation/amortisation pattern and expected sale/maturity of the hedged item and the hedging instrument.

For any risk exposure for which an entity elects to apply hedge accounting, the entity also makes the disclosures required by IFRS 7 *Financial Instruments: Disclosures* related to hedge accounting. The Committee noted, in particular, that paragraphs 22A–22C of IFRS 7 require the disclosure of information about an entity's risk management strategy and how it is applied to manage risk.

The Committee concluded that the requirements in IFRS 9 provide an adequate basis for an entity to determine whether foreign currency risk can be a separately identifiable and reliably measurable risk component of a non-financial asset held for consumption that an entity can designate as the hedged item in a fair value hedge accounting relationship. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Compensation for Delays or Cancellations (IFRS 15 Revenue from Contracts with Customers)—Agenda Paper 8

The Committee received a request about an airline's obligation to compensate customers for delayed or cancelled flights. In the fact pattern described in the request:

- a. legislation gives a flight passenger (customer) the right to be compensated by the flight provider (entity) for delays and cancellations subject to specified conditions in the legislation. The legislation stipulates the amount of compensation, which is unrelated to the amount the customer pays for a flight.
- b. the legislation creates enforceable rights and obligations, and forms part of the terms of a contract between the entity and a customer.
- c. applying IFRS 15 to a contract with a customer, the entity identifies as a performance obligation its promise to transfer a flight service to the customer.

The request asked whether the entity accounts for its obligation to compensate customers either: (a) as variable consideration applying paragraphs 50–59 of IFRS 15; or (b) applying

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, separately from its performance obligation to transfer a flight service to the customer.

Paragraph 47 of IFRS 15 requires an entity to ‘consider the terms of the contract and its customary business practices in determining the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer...The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both’. Paragraph 51 of IFRS 15 lists examples of common types of variable consideration—‘discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties or other similar items’.

Paragraph B33 of IFRS 15 specifies requirements for an entity’s obligation to pay compensation to a customer if its products cause harm or damage. An entity accounts for such an obligation applying IAS 37, separately from its performance obligation in the contract with the customer.

The Committee observed that, in the fact pattern described in the request, the entity promises to transport the customer from one specified location to another within a specified time period after the scheduled flight time. If the entity fails to do so, the customer is entitled to compensation. Accordingly, any compensation for delays or cancellations relates directly to the entity’s performance obligation; it does not represent compensation for harm or damage caused by the entity’s products as described in paragraph B33. The fact that legislation, rather than the contract, stipulates the compensation payable does not affect the entity’s determination of the transaction price—the compensation gives rise to variable consideration in the same way that penalties for delayed transfer of an asset gives rise to variable consideration as illustrated in Example 20 of the Illustrative Examples accompanying IFRS 15.

Consequently, the Committee concluded that compensation for delays or cancellations, as described in the request, is variable consideration in the contract. Accordingly, the entity applies the requirements in paragraphs 50–59 of IFRS 15 in accounting for its obligation to compensate customers for delays or cancellations. The Committee did not consider the question of whether the amount of compensation recognised as a reduction of revenue is limited to reducing the transaction price to nil.

The Committee concluded that the principles and requirements in IFRS 15 provide an adequate basis for an entity to determine its accounting for obligations to compensate customers for delays or cancellations. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Lessee’s Incremental Borrowing Rate (IFRS 16 Leases)—Agenda Paper 2

The Committee received a request about the definition of a lessee’s incremental borrowing rate in IFRS 16. The request asked whether a lessee’s incremental borrowing rate is required to reflect the interest rate in a loan with both a similar maturity to the lease and a similar payment profile to the lease payments.

Applying IFRS 16, a lessee uses its incremental borrowing rate in measuring a lease liability when the interest rate implicit in the lease cannot be readily determined (paragraph 26 of IFRS 16). Appendix A to IFRS 16 defines a lessee’s incremental borrowing rate as ‘the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment’. The lessee’s incremental borrowing rate is therefore a lease-specific rate that the Board defined ‘to take into account the terms and conditions of the lease’ (paragraph BC162).

In determining its incremental borrowing rate, the Board explained in paragraph BC162 that, depending on the nature of the underlying asset and the terms and conditions of the lease, a lessee may be able to refer to a rate that is readily observable as a starting point. A lessee would then adjust such an observable rate as is needed to determine its incremental borrowing rate as defined in IFRS 16.

The Committee observed that the definition of a lessee's incremental borrowing rate requires a lessee to determine its incremental borrowing rate for a particular lease considering the terms and conditions of the lease, and determine a rate that reflects the rate it would have to pay to borrow:

- a. over a similar term to the lease term;
- b. with a similar security to the security (collateral) in the lease;
- c. the amount needed to obtain an asset of a similar value to the right-of-use asset arising from the lease; and
- d. in a similar economic environment to that of the lease.

The definition of a lessee's incremental borrowing rate in IFRS 16 does not explicitly require a lessee to determine its incremental borrowing rate to reflect the interest rate in a loan with a similar payment profile to the lease payments. Nonetheless, the Committee observed that, in applying judgement in determining its incremental borrowing rate as defined in IFRS 16, a lessee might often refer as a starting point to a readily observable rate for a loan with a similar payment profile to that of the lease.

The Committee concluded that the principles and requirements in IFRS 16 provide an adequate basis for a lessee to determine its incremental borrowing rate. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Lease Term and Useful Life of Leasehold Improvements (IFRS 16 Leases and IAS 16 Property, Plant and Equipment)—Agenda Paper 3

The Committee received a request about cancellable or renewable leases.

The cancellable lease described in the request is one that does not specify a particular contractual term but continues indefinitely until either party to the contract gives notice to terminate. The contract includes a notice period of, for example, less than 12 months and the contract does not oblige either party to make a payment on termination. The renewable lease described in the request is one that specifies an initial period, and renews indefinitely at the end of the initial period unless terminated by either of the parties to the contract.

The request asked two questions:

- a. how to determine the lease term of a cancellable lease or a renewable lease. Specifically, the request asked whether, when applying paragraph B34 of IFRS 16 and assessing 'no more than an insignificant penalty', an entity considers the broader economics of the contract, and not only contractual termination payments. Such considerations might include, for example, the cost of abandoning or dismantling leasehold improvements.
- b. whether the useful life of any related non-removable leasehold improvements is limited to the lease term determined applying IFRS 16. Non-removable leasehold improvements are, for example, fixtures and fittings acquired by the lessee and constructed on the underlying asset that is the subject of the cancellable or renewable lease. The lessee will use and benefit from the leasehold improvements only for as long as it uses the underlying asset.

Lease term

Paragraph 18 of IFRS 16 requires an entity to determine the lease term as the non-cancellable period of a lease, together with both (a) periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option; and (b) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option.

In determining the lease term and assessing the length of the non-cancellable period of a lease, paragraph B34 of IFRS 16 requires an entity to determine the period for which the contract is enforceable. Paragraph B34 specifies that 'a lease is no longer enforceable when the lessee and the lessor each has the right to terminate the lease without permission from the other party with no more than an insignificant penalty'.

Paragraph BC156 sets out the Board's view that 'the lease term should reflect an entity's reasonable expectation of the period during which the underlying asset will be used because that approach provides the most useful information'. Paragraph BC129 explains that, in the Board's view, an entity is unlikely to add a clause to a lease contract that does not have economic substance.

The Committee observed that, in applying paragraph B34 and determining the enforceable period of the lease described in the request, an entity considers:

- a. the broader economics of the contract, and not only contractual termination payments. For example, if either party has an economic incentive not to terminate the lease such that it would incur a penalty on termination that is more than insignificant, the contract is enforceable beyond the date on which the contract can be terminated; and
- b. whether each of the parties has the right to terminate the lease without permission from the other party with no more than an insignificant penalty. Applying paragraph B34, a lease is no longer enforceable only when both parties have such a right. Consequently, if only one party has the right to terminate the lease without permission from the other party with no more than an insignificant penalty, the contract is enforceable beyond the date on which the contract can be terminated by that party.

If an entity concludes that the contract is enforceable beyond the notice period of a cancellable lease (or the initial period of a renewable lease), it then applies paragraphs 19 and B37-B40 of IFRS 16 to assess whether the lessee is reasonably certain not to exercise the option to terminate the lease.

Useful life of non-removable leasehold improvements

Paragraph 50 of IAS 16 requires an item of property, plant and equipment (asset) to be depreciated over its useful life.

IAS 16 defines the useful life of an asset as (*emphasis added*) 'the period over which an asset is expected to be available for use by an entity; or the number of production or similar units expected to be obtained from the asset by an entity'.

Paragraphs 56 and 57 of IAS 16 provide further requirements on the useful life of an asset. In particular, paragraph 56(d) specifies that in determining the useful life of an asset, an entity considers any legal or similar limits on the use of the asset, such as the expiry dates of related leases. Paragraph 57 specifies that the useful life of an asset (a) is defined in terms of the asset's expected utility to the entity, and (b) may be shorter than its economic life.

An entity applies paragraphs 56-57 of IAS 16 in determining the useful life of non-removable leasehold improvements. If the lease term of the related lease is shorter than the economic life of those leasehold improvements, the entity considers whether it expects to use the leasehold

improvements beyond that lease term. If the entity does not expect to use the leasehold improvements beyond the lease term of the related lease then, applying paragraph 57 of IAS 16, it concludes that the useful life of the non-removable leasehold improvements is the same as the lease term. The Committee observed that, applying paragraphs 56-57 of IAS 16, an entity might often reach this conclusion for leasehold improvements that the entity will use and benefit from only for as long as it uses the underlying asset in the lease.

Interaction between the determination of the useful life of non-removable leasehold improvements and the enforceable period of the lease and lease term

In assessing whether a lessee is reasonably certain to extend (or not to terminate) a lease, paragraph B37 of IFRS 16 requires an entity to consider all relevant facts and circumstances that create an economic incentive for the lessee. This includes significant leasehold improvements undertaken (or expected to be undertaken) over the term of the contract that are expected to have significant economic benefit for the lessee when an option to extend or terminate the lease becomes exercisable (paragraph B37(b)).

In addition, as noted above, an entity considers the broader economics of the contract when determining the enforceable period of a lease. This includes, for example, the costs of abandoning or dismantling non-removable leasehold improvements. If an entity expects to use non-removable leasehold improvements beyond the date on which the contract can be terminated, the existence of those leasehold improvements indicates that the entity might incur a more than insignificant penalty if it terminates the lease. Consequently, applying paragraph B34 of IFRS 16, an entity considers whether the contract is enforceable for at least the period of expected utility of the leasehold improvements.

The Committee concluded that the principles and requirements in IFRS 16 provide an adequate basis for an entity to determine the lease term of cancellable and renewable leases.

The Committee also concluded that the requirements in IAS 16 and IFRS 16 provide an adequate basis for an entity to determine the useful life of any non-removable leasehold improvements relating to such a lease. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Presentation of Liabilities or Assets Related to Uncertain Tax Treatments (IAS 1 Presentation of Financial Statements)—Agenda Paper 7

The Committee received a request about the presentation of liabilities or assets related to uncertain tax treatments recognised applying IFRIC 23 *Uncertainty over Income Tax Treatments* (uncertain tax liabilities or assets). The submitter asked whether, in its statement of financial position, an entity is required to present uncertain tax liabilities as current (or deferred) tax liabilities or, instead, within another line item such as provisions. A similar question could arise regarding uncertain tax assets.

The definitions in IAS 12 of current tax and deferred tax liabilities or assets

When there is uncertainty over income tax treatments, paragraph 4 of IFRIC 23 requires an entity to 'recognise and measure its current or deferred tax asset or liability applying the requirements in IAS 12 based on taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates determined applying IFRIC 23'. Paragraph 5 of IAS 12 *Income Taxes* defines:

- a. current tax as the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period; and

- b. deferred tax liabilities (or assets) as the amounts of income taxes payable (recoverable) in future periods in respect of taxable (deductible) temporary differences and, in the case of deferred tax assets, the carryforward of unused tax losses and credits.

Consequently, the Committee observed that uncertain tax liabilities or assets recognised applying IFRIC 23 are liabilities (or assets) for current tax as defined in IAS 12, or deferred tax liabilities or assets as defined in IAS 12.

Presentation of uncertain tax liabilities (or assets)

Neither IAS 12 nor IFRIC 23 contain requirements on the presentation of uncertain tax liabilities or assets. Therefore, the presentation requirements in IAS 1 apply. Paragraph 54 of IAS 1 states that 'the statement of financial position shall include line items that present: ... (n) liabilities and assets for current tax, as defined in IAS 12; (o) deferred tax liabilities and deferred tax assets, as defined in IAS 12...'.

Paragraph 57 of IAS 1 states that paragraph 54 'lists items that are sufficiently different in nature or function to warrant separate presentation in the statement of financial position'. Paragraph 29 requires an entity to 'present separately items of a dissimilar nature or function unless they are immaterial'.

Accordingly, the Committee concluded that, applying IAS 1, an entity is required to present uncertain tax liabilities as current tax liabilities (paragraph 54(n)) or deferred tax liabilities (paragraph 54(o)); and uncertain tax assets as current tax assets (paragraph 54(n)) or deferred tax assets (paragraph 54(o)).

The Committee concluded that the requirements in IFRS Standards provide an adequate basis for an entity to determine the presentation of uncertain tax liabilities and assets. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Disclosure of Changes in Liabilities Arising from Financing Activities (IAS 7 Statement of Cash Flows)—Agenda Paper 5–5A

The Committee received a request from users of financial statements (investors) about the disclosure requirements in IAS 7 that relate to changes in liabilities arising from financing activities. Specifically, investors asked whether the disclosure requirements in paragraphs 44B–44E of IAS 7 are adequate to require an entity to provide disclosures that meet the objective in paragraph 44A of IAS 7.

Meeting the disclosure objective (Paragraph 44A of IAS 7)

Paragraph 44A of IAS 7 requires an entity to provide 'disclosures that enable [investors] to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes'. To the extent necessary to satisfy this objective, paragraph 44B specifies that an entity discloses the following changes in liabilities arising from financing activities:

- a. changes from financing cash flows;
- b. changes arising from obtaining or losing control of subsidiaries or other businesses;
- c. the effect of changes in foreign exchange rates;
- d. changes in fair values; and
- e. other changes.

The Board explained in paragraph BC16 that it developed the disclosure objective in paragraph 44A to reflect the needs of investors, including those summarised in paragraph BC10. The Board also noted in paragraph BC18 that when considering whether it has fulfilled the objective in paragraph 44A, an entity takes into consideration the extent to which information about changes in liabilities arising from financing activities provides relevant information to investors, considering the needs of investors summarised in paragraph BC10. These investor needs are:

- a. to check their understanding of the entity's cash flows and use that understanding to improve their confidence in forecasting the entity's future cash flows;
- b. to provide information about the entity's sources of finance and how those sources have been used over time; and
- c. to help them understand the entity's exposure to risks associated with financing.

Consequently, the Committee concluded that, to meet the disclosure objective in paragraph 44A of IAS 7, an entity considers whether its disclosures enable investors to check their understanding of the entity's cash flows, to provide information about the entity's sources of finance and to help them understand the entity's exposure to risks associated with financing as described in paragraph BC10.

Reconciling between the opening and closing balances of liabilities arising from financing activities

Paragraph 44D of IAS 7 states that '[o]ne way to fulfil the disclosure requirement in paragraph 44A is by providing a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities, including the changes identified in paragraph 44B. When an entity discloses such a reconciliation, it shall provide sufficient information to enable investors to link items included in the reconciliation to the statement of financial position and the statement of cash flows'.

Consequently, when an entity discloses a reconciliation as described in paragraph 44D, the Committee observed that the entity provides information that enables investors to link items included in the reconciliation to other areas of the financial statements. In doing this, an entity applies:

- a. paragraph 44C to identify liabilities arising from financing activities and use them as the basis of the reconciliation. Paragraph 44C defines these liabilities as 'liabilities for which cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities'. If an entity also chooses to define, and reconcile, a different 'net debt' measure, this does not remove the requirement to identify the entity's liabilities arising from financing activities as defined in paragraph 44C.
- b. paragraph 44E to disclose changes in liabilities arising from financing activities separately from changes in any other assets and liabilities. Paragraph 44E states '[i]f an entity provides the disclosure required by paragraph 44A in combination with disclosures of changes in other assets and liabilities, it shall disclose the changes in liabilities arising from financing activities separately from changes in those other assets and liabilities'.
- c. paragraph 44D of IAS 7 to provide sufficient information to enable investors to link the items included in the reconciliation to amounts reported in the statement of financial position and the statement of cash flows, or related notes. An entity develops disclosures that enable investors to link (i) the opening and closing balances of the liabilities arising

from financing activities reported in the reconciliation, to (ii) amounts reported in the entity's statement of financial position (or related notes) regarding those liabilities.

The Committee also observed that an entity applies judgement in determining the extent to which it disaggregates and explains the changes in liabilities arising from financing activities included in the reconciliation, considering the investor information needs described in paragraph BC10. In this respect, the Committee noted the following:

- a. in disaggregating liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 30A of IAS 1 *Presentation of Financial Statements*. Paragraph 30A of IAS 1 states that '[a]n entity shall not reduce the understandability of its financial statements...by aggregating material items that have different natures or functions'. Accordingly, in considering the investor information needs in paragraph BC10, an entity discloses any individually material items separately in the reconciliation. Such items include material classes of liability (or asset) arising from financing activities and material reconciling items (ie cash or non-cash changes).
- b. in explaining liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 112(c) of IAS 1. Paragraph 112(c) of IAS 1 requires an entity to disclose 'information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them'. Accordingly, applying paragraphs 44A–44E an entity determines the appropriate structure for its reconciliation including the appropriate level of disaggregation. Thereafter, the entity determines whether additional explanation is needed to meet the disclosure objective in paragraph 44A. An entity would explain each class of liability (or asset) arising from financing activities included in the reconciliation and each reconciling item in a way that (i) provides information about its sources of finance, (ii) enables investors to check their understanding of the entity's cash flows, and (iii) enables investors to link items to the statement of financial position and the statement of cash flows, or related notes.

The Committee concluded that the requirements in IFRS Standards provide an adequate basis for an entity to disclose information about changes in liabilities arising from financing activities that enables investors to evaluate those changes. Accordingly, the Committee concluded that the disclosure requirements in paragraphs 44B–44E of IAS 7, together with requirements in IAS 1, are adequate to require an entity to provide disclosures that meet the objective in paragraph 44A of IAS 7. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Subsequent Expenditure on Biological Assets (IAS 41 Agriculture)—Agenda Paper 9

The Committee received a request about the accounting for costs related to the biological transformation (subsequent expenditure) of biological assets measured at fair value less costs to sell applying IAS 41. The request asked whether an entity capitalises subsequent expenditure (ie adds it to the carrying amount of the asset) or, instead, recognises subsequent expenditure as an expense when incurred.

The Committee observed that capitalising subsequent expenditure or recognising it as an expense has no effect on the measurement of biological assets nor does it have any effect on profit or loss; however, it affects the presentation of amounts in the statement of profit or loss.

IAS 41 does not specify requirements on the accounting for subsequent expenditure. Paragraph B62 of the Basis for Conclusions on IAS 41 explains that ‘...the [IASB] Board decided not to explicitly prescribe the accounting for subsequent expenditure related to biological assets in the Standard, because it believes to do so is unnecessary with a fair value measurement approach’.

Accordingly, the Committee concluded that, applying IAS 41, an entity either capitalises subsequent expenditure or recognises it as an expense when incurred. Applying paragraph 13 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, an entity would apply its accounting policy for subsequent expenditure consistently to each group of biological assets. An entity would also disclose the selected accounting policy applying paragraphs 117–124 of IAS 1 *Presentation of Financial Statements* if that disclosure would assist users of financial statements in understanding how those transactions are reflected in reported financial performance.

In the light of its analysis, the Committee considered whether to add a project to its standard-setting agenda on the accounting for subsequent expenditure on biological assets. The Committee has not [yet] obtained evidence to suggest that standard-setting on this matter at this time would result in an improvement to financial reporting that would be sufficient to outweigh the costs. The Committee therefore [decided] not to add the matter to its standard-setting agenda.

Committee's agenda decisions

The process for publishing an agenda decision might often result in explanatory material that provides new information that was not otherwise available and could not otherwise reasonably have been expected to be obtained. Because of this, an entity might determine that it needs to change an accounting policy as a result of an agenda decision. The Board expects that an entity would be entitled to sufficient time to make that determination and implement any change (for example, an entity may need to obtain new information or adapt its systems to implement a change).

The Committee discussed the following matters and decided not to add them to its standard-setting agenda.

Holdings of Cryptocurrencies—Agenda Paper 12

The Committee discussed how IFRS Standards apply to holdings of cryptocurrencies.

The Committee noted that a range of cryptoassets exist. For the purposes of its discussion, the Committee considered a subset of cryptoassets with all the following characteristics that this agenda decision refers to as a 'cryptocurrency':

- a. a digital or virtual currency recorded on a distributed ledger that uses cryptography for security.
- b. not issued by a jurisdictional authority or other party.
- c. does not give rise to a contract between the holder and another party.

Nature of a cryptocurrency

Paragraph 8 of IAS 38 *Intangible Assets* defines an intangible asset as 'an identifiable non-monetary asset without physical substance'.

Paragraph 12 of IAS 38 states that an asset is identifiable if it is separable or arises from contractual or other legal rights. An asset is separable if it 'is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability'.

Paragraph 16 of IAS 21 *The Effects of Changes in Foreign Exchange Rates* states that 'the essential feature of a non-monetary item is the absence of a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency'.

The Committee observed that a holding of cryptocurrency meets the definition of an intangible asset in IAS 38 on the grounds that (a) it is capable of being separated from the holder and sold or transferred individually; and (b) it does not give the holder a right to receive a fixed or determinable number of units of currency.

Which IFRS Standard applies to holdings of cryptocurrencies?

The Committee concluded that IAS 2 *Inventories* applies to cryptocurrencies when they are held for sale in the ordinary course of business. If IAS 2 is not applicable, an entity applies IAS 38 to holdings of cryptocurrencies. The Committee considered the following in reaching its conclusion.

Intangible Asset

IAS 38 applies in accounting for all intangible assets except:

- a. those that are within the scope of another Standard;
- b. financial assets, as defined in IAS 32 *Financial Instruments: Presentation*;
- c. the recognition and measurement of exploration and evaluation assets; and
- d. expenditure on the development and extraction of minerals, oil, natural gas and similar non-regenerative resources.

Accordingly, the Committee considered whether a holding of cryptocurrency meets the definition of a financial asset in IAS 32 or is within the scope of another Standard.

Financial asset

Paragraph 11 of IAS 32 defines a financial asset. In summary, a financial asset is any asset that is: (a) cash; (b) an equity instrument of another entity; (c) a contractual right to receive cash or another financial asset from another entity; (d) a contractual right to exchange financial assets or financial liabilities with another entity under particular conditions; or (e) a particular contract that will or may be settled in the entity's own equity instruments.

The Committee concluded that a holding of cryptocurrency is not a financial asset. This is because a cryptocurrency is not cash (see below). Nor is it an equity instrument of another entity. It does not give rise to a contractual right for the holder and it is not a contract that will or may be settled in the holder's own equity instruments.

Cash

Paragraph AG3 of IAS 32 states that 'currency (cash) is a financial asset because it represents the medium of exchange and is therefore the basis on which all transactions are measured and recognised in financial statements. A deposit of cash with a bank or similar financial institution is a financial asset because it represents the contractual right of the depositor to obtain cash from the institution or to draw a cheque or similar instrument against the balance in favour of a creditor in payment of a financial liability'.

The Committee observed that the description of cash in paragraph AG3 of IAS 32 implies that cash is expected to be used as a medium of exchange (ie used in exchange for goods or services) and as the monetary unit in pricing goods or services to such an extent that it would be the basis on which all transactions are measured and recognised in financial statements.

Some cryptocurrencies can be used in exchange for particular good or services. However, the Committee noted that it is not aware of any cryptocurrency that is used as a medium of exchange and as the monetary unit in pricing goods or services to such an extent that it would be the basis on which all transactions are measured and recognised in financial statements. Consequently, the Committee concluded that a holding of cryptocurrency is not cash because cryptocurrencies do not currently have the characteristics of cash.

Inventory

IAS 2 applies to inventories of intangible assets. Paragraph 6 of that Standard defines inventories as assets:

- a. held for sale in the ordinary course of business;
- b. in the process of production for such sale; or
- c. in the form of materials or supplies to be consumed in the production process or in the rendering of services.

The Committee observed that an entity may hold cryptocurrencies for sale in the ordinary course of business. In that circumstance, a holding of cryptocurrency is inventory for the entity and, accordingly, IAS 2 applies to that holding.

The Committee also observed that an entity may act as a broker-trader of cryptocurrencies. In that circumstance, the entity considers the requirements in paragraph 3(b) of IAS 2 for commodity broker-traders who measure their inventories at fair value less costs to sell. Paragraph 5 of IAS 2 states that broker-traders are those who buy or sell commodities for others or on their own account. The inventories referred to in paragraph 3(b) are principally acquired with the purpose of selling in the near future and generating a profit from fluctuations in price or broker-traders' margin.

Disclosure

In addition to disclosures otherwise required by IFRS Standards, an entity is required to disclose any additional information that is relevant to an understanding of its financial statements (paragraph 112 of IAS 1 *Presentation of Financial Statements*). In particular, the Committee noted the following disclosure requirements in the context of holdings of cryptocurrencies:

- a. An entity provides the disclosures required by (i) paragraphs 36–39 of IAS 2 for cryptocurrencies held for sale in the ordinary course of business; and (ii) paragraphs 118–128 of IAS 38 for holdings of cryptocurrencies to which it applies IAS 38.
- b. If an entity measures holdings of cryptocurrencies at fair value, paragraphs 91–99 of IFRS 13 *Fair Value Measurement* specify applicable disclosure requirements.
- c. Applying paragraph 122 of IAS 1, an entity discloses judgements that its management has made regarding its accounting for holdings of cryptocurrencies if those are part of the judgements that had the most significant effect on the amounts recognised in the financial statements.
- d. Paragraph 21 of IAS 10 *Events after the Reporting Period* requires an entity to disclose details of any material non-adjusting events, including information about the nature of the event and an estimate of its financial effect (or a statement that such an estimate cannot be made). For example, an entity holding cryptocurrencies would consider whether changes in the fair value of those holdings after the reporting period are of such significance that non-disclosure could influence the economic decisions that users of financial statements make on the basis of the financial statements.

Costs to Fulfil a Contract (IFRS 15 Revenue from Contracts with Customers)— Agenda Paper 10

The Committee received a request about the recognition of costs incurred to fulfil a contract as an entity satisfies a performance obligation in the contract over time. In the fact pattern described in the request, the entity (a) transfers control of a good over time (ie one (or more) of the criteria in paragraph 35 of IFRS 15 is met) and, therefore, satisfies a performance obligation and recognises revenue over time; and (b) measures progress towards complete satisfaction of the performance obligation using an output method applying paragraphs 39–43 of IFRS 15. The entity incurs costs in constructing the good. At the reporting date, the costs incurred relate to construction work performed on the good that is transferring to the customer as the good is being constructed.

The Committee first noted the principles and requirements in IFRS 15 relating to the measurement of progress towards complete satisfaction of a performance obligation satisfied over time. Paragraph 39 states that ‘the objective when measuring progress is to depict an entity’s performance in transferring control of goods or services promised to a customer’. The Committee also observed that when evaluating whether to apply an output method to measure progress, paragraph B15 requires an entity to ‘consider whether the output selected would faithfully depict the entity’s performance towards complete satisfaction of the performance obligation’.

In considering the recognition of costs, the Committee noted that paragraph 98(c) of IFRS 15 requires an entity to recognise as expenses when incurred ‘costs that relate to satisfied performance obligations (or partially satisfied performance obligations) in the contract (ie costs that relate to past performance)’.

The Committee observed that the costs of construction described in the request are costs that relate to the partially satisfied performance obligation in the contract—ie they are costs that relate to the entity’s past performance. Those costs do not, therefore, generate or enhance resources of the entity that will be used in continuing to satisfy the performance obligation in the future (paragraph 95(b)). Consequently, those costs do not meet the criteria in paragraph 95 of IFRS 15 to be recognised as an asset.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine how to recognise costs incurred in fulfilling a contract in the fact pattern described in the request. Consequently, the Committee decided not to add the matter to its standard-setting agenda.

Subsurface Rights (IFRS 16 Leases)—Agenda Paper 11

The Committee received a request about a particular contract for subsurface rights. In the contract described in the request, a pipeline operator (customer) obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration. The contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed. The landowner retains the right to use the surface of the land above the pipeline, but it has no right to access or otherwise change the use of the specified underground space throughout the 20-year period of use. The customer has the right to perform inspection, repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).

The request asked whether IFRS 16, IAS 38 *Intangible Assets* or another IFRS Standard applies in accounting for the contract.

Which IFRS Standard does an entity consider first?

Paragraph 3 of IFRS 16 requires an entity to apply IFRS 16 to all leases, with limited exceptions. Paragraph 9 of IFRS 16 states: 'At inception of a contract, an entity shall assess whether the contract is, or contains, a lease'.

The Committee observed that, in the contract described in the request, none of the exceptions in paragraphs 3 and 4 of IFRS 16 apply—in particular, the Committee noted that the underground space is tangible. Accordingly, if the contract contains a lease, IFRS 16 applies to that lease. If the contract does not contain a lease, the entity would then consider which other IFRS Standard applies.

The Committee therefore concluded that the entity first considers whether the contract contains a lease as defined in IFRS 16.

The definition of a lease

Paragraph 9 of IFRS 16 states that 'a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration'. Applying paragraph B9 of IFRS 16, to meet the definition of a lease the customer must have both:

- a. the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use; and
- b. the right to direct the use of the identified asset throughout the period of use.

Identified asset

Paragraphs B13–B20 of IFRS 16 provide application guidance on an identified asset. Paragraph B20 states that a 'capacity portion of an asset is an identified asset if it is physically distinct'. But 'a customer does not have the right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use' (paragraph B14).

The Committee observed that, in the contract described in the request, the specified underground space is physically distinct from the remainder of the land. The contract's specifications include the path, width and depth of the pipeline, thereby defining a physically distinct underground space. The space being underground does not in itself affect whether it is an identified asset—the specified underground space is physically distinct in the same way that a specified area of space on the land's surface would be physically distinct.

The landowner does not have the right to substitute the underground space throughout the period of use. Consequently, the Committee concluded that the specified underground space is an identified asset as described in paragraphs B13–B20.

Right to obtain substantially all the economic benefits from use

Paragraphs B21–B23 of IFRS 16 provide application guidance on the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use. Paragraph B21 specifies that a customer can have that right, for example, by having exclusive use of the identified asset throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to obtain substantially all the economic benefits from use of the specified underground space throughout the 20-year period of use. The customer has exclusive use of the specified underground space throughout that period of use.

Right to direct the use

Paragraphs B24-B30 of IFRS 16 provide application guidance on the right to direct the use of an identified asset throughout the period of use. Paragraph B24 specifies that a customer has that right if either:

- a. the customer has the right to direct how and for what purpose the asset is used throughout the period of use; or
- b. the relevant decisions about how and for what purpose the asset is used are predetermined and (i) the customer has the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions; or (ii) the customer designed the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to direct the use of the specified underground space throughout the 20-year period of use because the conditions in paragraph B24(b)(i) exist. How and for what purpose the specified underground space will be used (ie to locate the pipeline with specified dimensions through which oil will be transported) is predetermined in the contract. The customer has the right to operate the specified underground space by having the right to perform inspection, repairs and maintenance work. The customer makes all the decisions about the use of the specified underground space that can be made during the 20-year period of use.

Consequently, the Committee concluded that the contract described in the request contains a lease as defined in IFRS 16. The customer would therefore apply IFRS 16 in accounting for that lease.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine its accounting for the contract described in the request. Consequently, the Committee decided not to add the matter to its standard-setting agenda.

Effect of a Potential Discount on Plan Classification (IAS 19 Employee Benefits)— Agenda Paper 13

The Committee received a request about the classification of a post-employment benefit plan applying IAS 19. In the fact pattern described in the request, an entity sponsors a post-employment benefit plan that is administered by a third party. The relevant terms and conditions of the plan are as follows:

- a. the entity has an obligation to pay fixed annual contributions to the plan. The entity has determined that it will have no legal or constructive obligation to pay further contributions if the plan does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.
- b. the entity is entitled to a potential discount on its annual contributions. The discount arises if the ratio of plan assets to plan liabilities exceeds a set level. Thus, any discount might be affected by actuarial assumptions and the return on plan assets.

The request asked whether, applying IAS 19, the existence of a right to a potential discount would result in a defined benefit plan classification.

Paragraph 8 of IAS 19 defines defined contribution plans as ‘post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods’. Defined benefit plans are ‘post-employment benefit plans other than defined contribution plans’.

Paragraphs 27–30 of IAS 19 specify requirements relating to the classification of post-employment benefit plans as either defined contribution plans or defined benefit plans.

Paragraph 27 states that ‘[p]ost-employment benefit plans are classified as either defined contribution or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions’. The Committee therefore noted the importance of assessing all relevant terms and conditions of a post-employment benefit plan, as well as any informal practices that might give rise to a constructive obligation, in classifying the plan. That assessment would identify whether:

- a. the entity’s legal or constructive obligation towards employees is limited to the amount that it agrees to contribute to the fund (a defined contribution plan as described in paragraph 28); or
- b. the entity has an obligation to provide the agreed benefits to current and former employees (a defined benefit plan as described in paragraph 30).

The Committee noted that, in the fact pattern described in the request, assessing the relevant terms and conditions of the plan would include, for example, assessing (a) the manner and frequency in which annual contributions and any potential discount (including the target ratio) are determined; and (b) whether the manner and frequency of determining the contributions and any discount transfers actuarial risk and investment risk (as described in IAS 19) to the entity.

The Committee observed that, to meet the definition of a defined contribution plan, an entity must (a) have an obligation towards employees to pay fixed contributions into a fund; and (b) not be obliged to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current or prior periods. For example, there should be no possibility that future contributions could be set to cover shortfalls in funding employee benefits relating to employee service in the current and prior periods.

The Committee also observed that paragraphs 28 and 30 of IAS 19 specify that, under defined contribution plans, actuarial risk and investment risk fall in substance on the employee whereas, under defined benefit plans, those risks fall in substance on the entity. Paragraphs 28 and 30 describe (a) actuarial risk as the risk that benefits will cost the entity more than expected or will be less than expected for the employee; and (b) investment risk as the risk that assets invested will be insufficient to meet expected benefits. Paragraph BC29 of IAS 19 explains that the definition of defined contribution plans does not exclude the upside potential that the cost to the entity may be less than expected.

Consequently, the Committee concluded that, applying IAS 19, the existence of a right to a potential discount would not in itself result in classifying a post-employment benefit plan as a defined benefit plan. Nonetheless, the Committee reiterated the importance of assessing all relevant terms and conditions of a plan, as well as any informal practices that might give rise to a constructive obligation, in classifying the plan.

The Committee noted that, applying paragraph 122 of IAS 1 *Presentation of Financial Statements*, an entity would disclose the judgements that its management has made regarding the classification of post-employment benefit plans, if those are part of the judgements that had the most significant effect on the amounts recognised in the financial statements.

The Committee concluded that the requirements in IAS 19 provide an adequate basis for an entity to determine the classification of a post-employment benefit plan as a defined contribution plan or a defined benefit plan. Consequently, the Committee decided not to add the matter to its standard-setting agenda.

Items on the current agenda

Sale of a Single Asset Entity Containing Real Estate (IFRS 10 Consolidated Financial Statements)—Agenda Paper 6

The Committee received a request about the accounting for a transaction in which an entity, as part of its ordinary activities, enters into a contract with a customer to sell real estate by selling its equity interest in a subsidiary. The entity established the subsidiary some time before it enters into the contract with the customer; the subsidiary has one asset—real estate inventory—and a related tax asset or liability. The entity has applied IFRS 10 in consolidating the subsidiary before it loses control of the subsidiary as a result of the transaction with the customer.

The Committee did not make any decisions and will continue its discussion of the matter at a future meeting.

Lack of Exchangeability (IAS 21 The Effects of Changes in Foreign Exchange Rates)—Agenda Papers 14–14C

The Committee continued its discussion of possible narrow-scope standard-setting aimed at addressing situations in which exchangeability between two currencies is lacking.

The Committee decided to recommend that the Board propose narrow-scope amendments to IAS 21. The proposed narrow-scope amendments would:

- a. define exchangeability and a lack of exchangeability; and
- b. when exchangeability between two currencies is lacking, specify how an entity would determine the spot exchange rate and the disclosures it would provide.

Next step

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

Other matters

Matters Reported to the Board—Agenda Paper 15

The Committee received a report on matters that had previously been reported to the Board.

Committee Work in Progress—Agenda Paper 16

The Committee received a report on two requests for consideration at a future meeting. The Committee will discuss these requests at a future meeting.