IASB Update

From the International Accounting Standards Board

March 2011

Welcome to IASB Update

This IASB Update is a staff summary of the tentative decisions reached by the Board at a public meeting. As a project progresses, the Board can, and sometimes does, modify its earlier tentative decisions. Tentative decisions do not change existing requirements until those decisions are incorporated in a new or amended standard.

The IASB met in London on Monday 14 March to Friday 18 March. The FASB joined the IASB for many of the sessions, via video from its offices in Norwalk.

Most of the discussions focused on their three major MoU projects: revenue recognition, leases and insurance contracts. The sessions included two presentations on insurance contracts presented by external visitors.

The IASB also finalised effective dates for three of its new standards and held non-decision making discussions about impairment of financial assets.

Members of the Board met with representatives of the EFRAG Technical Expert Group (TEG) in a public meeting. They discussed revenue recognition, leases, financial instruments, insurance contracts, European outreach and EFRAG's pro-active agenda.

The IASB is holding a joint meeting with the FASB in the week beginning 21 March at the FASB's offices in Norwalk, Connecticut. The meeting will be webcast in the normal manner.

The topics discussed at the joint IASB/FASB board meeting were:

The topics discussed at the IASB Board meeting were:

Contact us

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

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

Future Board meetings

The IASB meets at least once a month for up to five days.

The next Board meetings in 2011 are:

21-23 March (joint meeting in Norwalk, US)
28-29 March
5-6 April (tentative)
11-15 April

To see all Board meetings for 2011, click here.

Archive of IASB Update Newsletter

Click here for archived copies of past issues of IASB Update on the IASB website.

Podcast summaries

To listen to a short Board meeting audio summary (podcast) or previous Board meetings, click here.

Sessions held jointly with the FASB

Fair value measurement - effective dates

The IASB discussed the effective date of an IFRS on fair value measurement in the light of the feedback received on the Request for Views *Effective Date and Transition Methods*.

The IASB tentatively decided that the effective date of an IFRS on fair value measurement should be 1 January 2013. That effective date would give entities (including those in emerging and transition economies) enough time to analyse the requirements and to make any necessary systems changes. It would also allow enough time for translation and for introducing the mandatory requirements into law. Tweleve Board members supported the proposed date, one preferred an earlier date, one a later date and one Board member was not present when the vote was taken.

The IASB also tentatively decided that early application should be permitted, in conformity with the proposal in the exposure draft. That would allow entities to apply the measurement and disclosure requirements as soon as practicable, thereby improving comparability in measurement and transparency in disclosures. It would also improve comparability with entities applying US GAAP. The decision was supported by all Board members present.

The IASB plans to issue an IFRS on fair value measurement in April 2011.

Financial instruments: hedge accounting

Hedge accounting is the third phase of the IASB's comprehensive project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. In December 2010 the Board published the exposure draft (ED) *Hedge Accounting*. The comment period for the ED ended on 9 March.

At this meeting the Board resumed this project phase following the public consultation period and discussed the:

- outreach summary
- comment letter summary

The Board received 233 comment letters. There was strong support for the proposals, with respondents welcoming the Board's approach of addressing hedge accounting comprehensively. They also agree with the principle-based approach proposed in the exposure draft, with many commenting that they thought that the proposal would resolve many of today's practice problems in applying IAS 39 *Financial Instruments: Recognition and Measurement*.

The Board was not asked to make any decisions at this meeting.

Insurance contracts

The IASB and FASB continued their discussions on insurance contracts by considering the following topics: alternative presentation models, allocation of the composite margin in profit and loss, whether the boards should permit or require a practical expedient for the discount rate, education sessions on the risk adjustment and on an alternative approach to deriving a discount rate, the discount rate for participating contracts, the timing of initial recognition and the definition of an insurance contract.

Alternative presentation models

The boards discussed several presentation approaches for the performance statement for insurers. The boards directed the staff to seek input on these approaches from the Insurance Working Group and from other users of insurance financial statements to help the boards to understand which approaches are most likely to meet the needs of users and whether those approaches would cause practical difficulties for the preparers of the financial statements.

The boards were not asked to make any decisions on this topic.

Composite margin-examples of run-off patterns

The boards considered alternative ways by which the composite margin could be allocated through profit or loss ('run off') in the statement of comprehensive income.

The boards were not asked to make any decisions on this topic.

Practical expedient for the discount rate

The boards discussed whether a practical expedient should be provided for determining the discount rate for a particular subset of entities.

The boards tentatively decided not to provide a practical expedient for determining the discount rate. Fourteen IASB members supported this decision, and one voted against.

The majority of the FASB members also supported this decision but noted that they would review this issue when they considered the scope and definition, particularly if those decisions would lead to contracts issued by non-financial institutions being within the scope of the standard.

Discount rate for participating contracts

The boards discussed the discount rate for insurance contracts that contain participating features. The boards tentatively decided to:

a. clarify that the objective of the discount rate used to measure participating insurance contracts should be consistent with the discount rate used to measure non-participating insurance contracts.
b. provide guidance that to the extent that the amount, timing or uncertainty of the cash flows arising from an insurance contract depend wholly or partly on the performance of specific assets, the insurer should adjust those cash flows using a discount rate that reflects that dependency.

All the IASB and FASB members supported this decision.

Recognition

The boards tentatively decided that insurance contract assets and liabilities should initially be recognised when the coverage period begins, and to require the recognition of an onerous contract liability in the pre-coverage period if management becomes aware of onerous contracts in the pre-coverage period. All the FASB members and ten IASB members supported this decision (five voted against).

Definition of an insurance contract

The IASB's exposure draft (ED) *Insurance Contracts* and the FASB's Discussion Paper *Preliminary Views on Insurance Contracts* (DP) proposed to define an insurance contract as 'a contract under which one party accepts significant insurance risk from another party by agreeing to compensate the policyholder if a specified uncertain future event adversely affects the policyholder'. The boards tentatively decided to confirm the proposal in the ED and DP that:

a. an insurer should consider the time value of money in assessing whether the additional benefits payable in any scenario are significant.

b. a contract does not transfer significant insurance risk if there is no scenario that has commercial substance in which the insurer can suffer a loss, with loss defined as an excess of the present value of net cash outflows over the present value of the premiums.

All the FASB members and twelve IASB members supported this decision (three voted against).

Next steps

The boards will continue their discussion on this project at their joint meeting in the week of 21 March 2011.

Education session on the risk margin

The IASB and FASB invited a guest speaker to provide an education session on how in practice a risk margin is calculated using a cost of capital approach and the linkage to the determination of the best estimate liabilities. The external presenter was Joachim Oechslin from Munich Re. The discussion will be continued on 22 March 2011 with presentations by other guest speakers.

The boards were not asked to make any decisions on this topic.

Education session on an alternative approach to deriving a discount rate

The IASB and FASB invited guest speakers to present an approach that derives a yield curve for a discount rate for all cash flows expected at a given duration by:

- identifying those liability cash flows that are matched in duration with the cash flows from the insurer's existing asset portfolio
- considering the reinvestment needs for cash flows that are not matched in duration, and
- considering the effect of options and guarantees embedded in the liabilities.

The external presenters were Jean-Michel Pinton and Baptiste Brechot from CNP Assurances and Eric Meistermann, from Deloitte.

The boards were not asked to make any decisions on this topic.

Leases

The IASB and the FASB discussed how to distinguish between a lease and a purchase or a sale, the accounting for purchase options, and short-term leases.

Distinguishing between a lease and a purchase or a sale

The boards discussed whether the leases standard should provide guidance for distinguishing a lease from a purchase or a sale.

The boards tentatively decided that guidance should not be provided in the leases standard for distinguishing a lease of an underlying asset from a purchase or a sale of an underlying asset. That is, if an arrangement does not contain a lease, it should be accounted for in accordance with other applicable standards (for example, property, plant, and equipment or revenue recognition). The IASB voted 11 in favour and 4 against, while the FASB voted unanimously in favour.

Accounting for purchase options

The boards discussed how lessees and lessors should account for options to purchase the underlying assets that are included within an arrangement that contains a lease.

The boards tentatively decided that lessees and lessors should include the exercise price of a purchase option (including bargain purchase options) in the measurement of the lessee's liability to make lease payments and the lessor's right to receive lease payments, if the lessee has a significant economic incentive to exercise the purchase option. If it is determined that the lessee has a significant economic incentive to exercise the purchase option, the right-of-use asset recognised by the lessee should be amortised over the economic life of the underlying asset, rather than over the lease term. The IASB voted 13 in favour and 2 against, while the FASB voted unanimously in favour.

The boards also discussed whether a lessee and a lessor should reassess how to account for a purchase option included within an arrangement that contains a lease in subsequent periods. The boards tentatively indicated a preference for specifying the same reassessment guidance for purchase options as was tentatively decided for options to extend or terminate a lease. However, the boards instructed the staff to seek input through targeted outreach on the costs and benefits of requiring reassessment.

The boards will continue their redeliberations of the *Leases* exposure draft at future meetings.

Short-term leases

The IASB and the FASB discussed the accounting for short-term leases by lessees and lessors. The boards tentatively decided that:

1. A short-term lease, for both lessees and lessors, is defined as 'a lease that, at the date of commencement of the lease, has a maximum possible term, including any options to renew, of 12 months or less'. The IASB and the FASB both voted unanimously in favour.
2. Lessees and lessors may elect:
    - as an accounting policy for a class of underlying asset(s) (the IASB voted 8 in favour and 7 against, while the FASB voted 5 in favour and 2 against), to account for all short-term leases by not recognising lease assets or lease liabilities (the IASB voted 10 in favour and 5 against, while the FASB voted 4 in favour and 3 against); and
    - to recognise lease payments in profit or loss on a straight-line basis over the lease term, unless another systematic and rational basis is more representative of the time pattern in which use is derived from the underlying asset. All the IASB and FASB members supported this decision.

Next steps

The boards will continue their redeliberations of the *Leases* exposure draft at the meeting in the week beginning 21 March.

IASB-only sessions

Impairment - education session

The IASB held an education session to discuss how to estimate expected losses and the impairment of purchased debt securities. No decisions were made at this meeting. The Board will discuss these issues jointly with the FASB at next week's joint board meeting.

Effective dates - post-employment benefits and other comprehensive income

The IASB met to confirm the effective date and transitional provisions in the light of the more general consultation being undertaken by the Board on effective dates.

The Board unanimously confirmed that the other comprehensive income amendments would be effective from 1 January 2012 and that the post-employment benefits amendments would be effective from 1 January 2013.

Sweep issues - forthcoming IFRS 12 *Disclosure of Interests in Other Entities*

The Board discussed a sweep issue that was raised by one board member during the drafting of IFRS 12 *Disclosure of Interests in Other Entities*. The board member was concerned that the risk disclosures did not adequately address situations in which an entity 'stepped in' to provide financial support to structured entities with which it had previously been involved, but in which it did not have any interest before providing the financial support.

The Board agreed that the final disclosure standard would clarify that, to meet the disclosure objective for risks associated with interests in unconsolidated structured entities, an entity should provide information about its exposure to risk from involvement that it had with unconsolidated structured entities in previous periods (eg sponsoring the structured entity), even if the entity no longer has any contractual involvement with the structured entity at the end of the reporting period.

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