NEWSLETTER OF THE INTERNATIONAL FINANCIAL REPORTING INTERPRETATIONS COMMITTEE

IASB IFRIC UPDATE

July 2003

The International Financial Reporting Interpretations Committee met on 1 and 2 July 2003 in London.

Agenda items

The IFRIC discussed the following agenda items:

Changes in decommissioning, restoration and similar liabilities

The IFRIC considered a revised draft Interpretation and discussed the following:

The IASB's consideration of the draft Interpretation

The IFRIC considered the IASB's discussion of the draft Interpretation in May 2003 and its recommendation that the IFRIC proceed with publishing an Exposure Draft.

The IFRIC also considered the IASB's recommendations that the IFRIC should be clear that:

(a) in the spirit of convergence and in reaching its consensus, it did consider US GAAP and why it decided not to adopt the approach in Statement of Financial Accounting Standards No. 143 *Accounting for Asset Retirement Obligations*.

(b) the scope of the draft Interpretation addresses only changes in estimated costs that fall within the scope of IAS 16 *Property, Plant and Equipment* and are recognised as a liability in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

The draft Basis for Conclusions

In addition to the IASB's recommendations, the IFRIC asked the staff to explain in the draft Basis for Conclusions:

(a) the interaction of the requirements in the Exposure Draft of proposed Improvements to IAS 16 and the approach taken in the draft Interpretation, in particular:

   (i) paragraph 20A and accounting for costs to dismantle and remove an asset and restore its site.

   (ii) paragraph 29 and the allowed alternative treatment. For example, when an entity chooses to carry the asset at a revalued amount.

   (iii) paragraph 27 of the Exposure Draft of revised IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Specifically, accounting for a change in estimate.

(b) why the draft Interpretation does not contain disclosure requirements, namely, because IAS 16 paragraph 63(b) and IAS 37 paragraphs 84 and 85 contain sufficient disclosure requirements.

Transition

The IFRIC agreed that the proposed Interpretation should be applied retrospectively because it is consistent with the transitional requirements in IAS 37 and IFRS 1 *First-time Adoption of International Financial Reporting Standards*. The IFRIC agreed to include an illustrative example of retrospective application for existing IFRS preparers and entities adopting IFRSs for the first time.

At the conclusion of its discussion, the IFRIC agreed to publish an Exposure Draft of the Interpretation.

IAS 19 *Employee Benefits*: Multi-employer plans

The IFRIC considered a draft Interpretation that (a) clarified when plans would meet the definition of a multi-employer plan; (b) explained how participants in multi-employer plans should apply defined benefit accounting; and (c) in the light of the former, included some discussion of when sufficient information may or may not be available.

The IFRIC questioned whether the message given by the draft Interpretation was clear or whether the level of detail was such that the principles were obscured. There was also substantial debate over whether the right balance had been struck between exhorting entities to apply defined benefit accounting and accepting that sometimes (perhaps often) it would not be possible.

The IFRIC agreed to revise the draft Interpretation:

(a) to include a clear statement that entities should make every effort to apply defined benefit accounting.

Definition of a multi-employer plan

(b) to remove the existing material on benefit and contribution levels and replace it with a short discussion of the difference between a multi-employer plan and a multiple employer plan.

Application of defined benefit accounting to multi-employer plans

(c) to specify that when defined benefit accounting is applied to a multi-employer plan, the plan should be measured using assumptions that apply to the plan as a whole.

(d) to specify that, having measured the plan as a whole, it is then necessary to determine whether there is a consistent and reasonable basis of allocation of the plan across the participants, either for:

   (i) an allocation of the surplus/deficit and the components of cost or

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ISSN 1477-206X

IAS 19 *Employee Benefits*: Multi-employer plans *(continued)*

(ii) an allocation of the surplus/deficit only.

The allocation should, if possible, be based on the entity's expected future contribution levels compared with those of all of the participants in the plan. If it is not possible to determine what the future levels of contributions will be, then an allocation based on current contribution levels should be considered.

(e) if a reasonable and consistent basis can be found for allocating only the surplus/deficit, to specify that the total change in value of the entity's share of the surplus/deficit should be recognised immediately in the income statement.

Availability of information

(f) to specify that when IAS 19 states 'sufficient information is not available' it means 'sufficient information cannot be obtained', ie that an entity has to try to get the information.

(g) to note that it should be presumed that if the entity is one of a few dominant participants in a multi-employer plan, the entity will be able to obtain information about the plan as a whole on an IAS 19 basis.

(h) to note that, given (g), it will be rare for such participants in a plan not to be able at least to give substantial information about the plan in the notes to the financial statements as required by IAS 19 paragraph 30(c), even if they are unable to determine a consistent and reasonable basis for allocation.

A revised Interpretation will be brought to the next IFRIC meeting.

IAS 19 *Employee Benefits*: Plans that would be defined contribution plans but for the existence of a minimum return guarantee

The IFRIC has been considering how to account for a plan that would be a defined contribution plan but for the existence of a minimum return guarantee. The terms of the plan are that a contribution is made each year based on the employee's current salary and the employee receives a benefit (a lump sum or an annuity) equal to the contributions paid into the plan plus the return generated on the assets acquired. The employer guarantees a minimum return on the assets over the period to when the benefit is paid.

The IFRIC considered a draft Interpretation that stated that such plans are defined benefit plans under IAS 19 and explained how defined benefit accounting should be applied to such plans.

The IFRIC requested a few changes to the draft Interpretation and then gave an initial vote of approval. A pre-ballot draft will be circulated to the IFRIC shortly.

IAS 19 *Employee Benefits*: Allocation of benefits to periods of service

IAS 19 paragraph 67 requires benefits to be allocated to periods of service according to the benefit formula, unless the benefit formula allocates a materially higher level of benefit to later years of service in which case a straight-line allocation should be made. The IFRIC considered whether expected increases in salary should be taken into account in determining whether a benefit formula expressed in terms of current salary will give rise to materially higher levels of benefits in later years.

IAS 19 requires the measurement of plan liabilities to take into account expected future salaries. The IFRIC agreed that this requirement meant that, to achieve consistent accounting for the same benefits, however they are expressed in terms of a benefit formula, the assessment of whether higher levels of benefit are attributed to later years of service would also have to take into account expected future salaries. This was illustrated by a comparison of a current salary plan and a career average plan. However, the IFRIC believed that, conceptually, the allocation of current salary benefits should not reflect expected future salaries.

The IFRIC noted that the EITF had also recently considered the allocation of benefits to periods of service in relation to 'cash balance' plans, and had concluded that the allocation of benefits should not reflect expected future salaries, on the grounds that these plans are not pay-related plans. The IFRIC instructed the staff to investigate further why the EITF had come to that conclusion.

The IFRIC agreed that it should indicate to the IASB that, given the measurement requirements of IAS 19, to achieve consistent results for plans that provide the same economic benefits, the allocation of benefits expressed in terms of current salaries would have to reflect expected future salaries. The IFRIC agreed that it should ask the IASB whether this view would cause the IASB to reconsider whether to address the issue of whether the measurement of plan liabilities should reflect expected future salaries, while also being clear that it was not asking the IASB to extend its current project on IAS 19 beyond this one additional issue.

Decommissioning and environmental rehabilitation funds

The IFRIC continued its discussion from the April 2003 meeting on decommissioning and environmental rehabilitation funds and considered a draft Interpretation. It noted that the IASB had agreed to amend the scope of IAS 39 *Financial Instruments: Recognition and Measurement* to exclude "rights to payments to reimburse the entity for expenditure it is required to make to settle a liability which it has recognised as a provision under IAS 37".

The IFRIC noted that this proposed amendment to IAS 39 appeared to be sufficiently narrow to exclude reimbursements only in the situations desired. However, the IFRIC questioned whether reimbursements for a liability, which had been converted from a provision (because the timing and amount were no longer uncertain), should also be included in the exemption. The IFRIC agreed that this was intended and suggested that the IASB might wish to reconsider the drafting of the exemption.

The IFRIC agreed that the issues and consensus section of the Interpretation should be redrafted to collate into a single paragraph the paragraphs on applying IAS 27 *Consolidated Financial Statements and Accounting for Investments in Subsidiaries*, SIC-12 *Consolidation—Special Purpose Entities*, IAS 28 *Accounting for Investments in Associates* and IAS 31 *Financial Reporting of Interests in Joint Ventures*. This would allow more focus on the main issues.

The IFRIC discussed whether the asset should be measured at:

(a) the entity's share of the fair value of the net assets of the fund (with any potential obligation to make good defaults of other contributors being accounted for separately as a contingent liability) or

(b) the fair value of the reimbursement right (which would normally be lower than (a) because of the risks involved, such as the possibility that the contributor may be required to make good defaults of other contributors).

The IFRIC noted that it had already concluded that any potential obligation to make additional contributions should be dealt with as a separate liability (or contingent liability) and not as a deduction from the asset. Therefore, approach (a) should be used. The IFRIC also noted that this would be the most useful information to users. However, the IFRIC agreed that the Basis for Conclusions on the Interpretation should discuss the difference between this approach and approach (b).

The IFRIC agreed not to address the issue of how to account for contributions made in advance of incurring an obligation because it did not believe that such situations were common in practice.

The IFRIC directed the staff to bring to a future meeting a draft Interpretation reflecting these discussions.

Rights of use

The IFRIC continued its deliberations from its April 2003 meeting of its draft Interpretation *Determining whether an Agreement contains a Lease*.

Although the IFRIC agreed to make some minor amendments to its earlier draft Interpretation, it reaffirmed its view that there are three key elements that need to be present for an agreement to contain a lease:

(a) fulfilment of the agreement depends upon use of a specific item or items ('the asset')

(b) the agreement conveys a right to use the asset for a specific period that allows the purchaser to exclude others from using the asset

(c) the purchaser is obliged to make payments to the supplier for the time that the asset is made available rather than for actual use of the asset.

The IFRIC also confirmed its tentative conclusion at the April meeting that the assessment of whether an agreement contains a lease should be made at inception of the agreement and that only changes to the provisions of the agreement should result in that reassessment.

The IFRIC again discussed application of the second criterion to agreements in which purchasers have rights to acquire output. It had previously agreed that where a supplier had rights to acquire substantially all of the output of the asset, a right of use was conveyed. The IFRIC agreed to simplify the application of this criterion by specifying that a right of use would be conveyed when it was remote that parties other than purchaser would take more than a minor amount of the output of the asset.

A minority of the IFRIC continue to disagree that the criteria in the draft Interpretation are sufficient by themselves to determine whether an agreement for output conveys a right of use and therefore contains a lease. The majority of the IFRIC, however, agreed to proceed with the Interpretation and instructed the staff to prepare a pre-ballot draft for it to vote on at the September meeting.

No further discussion on this draft Interpretation is planned.

New agenda items

The IFRIC discussed the following new agenda items:

IAS 11 *Construction Contracts* – The criteria for combining and segmenting contracts.

The IFRIC had a preliminary discussion of the guidance for combining and segmenting contracts (including contract options and additions, and the impact they have on combining and/or segmenting) under IAS 11 and US GAAP in particular, SOP 81-1 *Accounting for Performance of Construction-Type and Certain Production-Type Contracts.*

For the next meeting, the IFRIC asked the staff to draft an Interpretation that provides guidance on the criteria in IAS 11 for segmenting and combining contracts.

Future meetings and requests for Interpretations

The IFRIC's meetings for the remainder of 2003 are expected to take place in London, UK, as follows:

30 September and 1 October

2 and 3 December

Meeting dates, tentative agendas and additional details about the next meeting will also be posted to the IASB Website at www.iasb.org.uk before the meeting. Interested parties may also submit requests for Interpretations through the IASB Website.