# IFRIC Update

From the International Financial Reporting Interpretations Committee

January 2010


*IFRIC Update is published as a convenience to the IASB's constituents. All conclusions reported are tentative and may be changed or modified at future IFRIC meetings.*

*Decisions become final only after the IFRIC has taken a formal vote on an Interpretation or Draft Interpretation, which is confirmed by the IASB.*

The IFRIC met in London on 7 and 8 January, when it discussed:



Other information


- Future IFRIC meetings 2010
- Past issues of IFRIC ***Update***


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## Accounting for production stripping costs

In November 2009, the IFRIC decided to add this issue to its agenda. At the January 2010 meeting, the IFRIC accepted the project plan for the proposed interpretation. The IFRIC then deliberated the scope of the proposed interpretation. The IFRIC decided to use the following wording for the scope concept:

*Accounting for the costs of removal of waste material in a surface mining activity during the production phase.*

The staff will present papers at the March 2010 meeting discussing the costs to be considered by this interpretation and related definition of costs within this project. The staff will also present papers discussing the accounting for such costs including recognition, measurement and attribution/ amortisation of any asset that may arise.

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## Vesting and non-vesting conditions

The IFRIC received a request to clarify the basis on which vesting conditions, especially performance conditions, can be distinguished from non-vesting conditions. Specifically, the IFRIC was asked how to distinguish between a service condition, a performance condition and a non-vesting condition. Two application issues were presented to the IFRIC:

- Does there need to be a direct link between a performance target and an individual employee's service in order for that target to be a performance condition?
- When determining whether the target qualifies as a performance condition, does it matter whether the specified service period is shorter or longer than the period over which the performance target should be met?

The IFRIC noted that there is a lack of clarity on the definition of vesting conditions and revised guidance included in *Vesting Conditions and Cancellations* (Amendment to IFRS 2) issued in January 2008. As such, divergent practices may result when distinguishing between vesting conditions and non-vesting conditions.

The IFRIC concluded that the consistency of application would be improved by clarifying the distinction between service conditions, performance conditions and non-vesting conditions. Therefore, the IFRIC decided to add the issue to its agenda and directed the staff to develop a paper for discussion at the March 2010 meeting.

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## Agenda decisions

*The following explanation is published for information only and does not change existing IFRS* *requirements. IFRIC agenda decisions are not Interpretations. IFRIC Interpretations are determined only after extensive deliberation and due process, including a formal vote. IFRIC Interpretations become final only when approved by the IASB.*

***IFRS 2 Share-based Payment*** - Transactions in which the manner of settlement is contingent on future events

The IFRIC received a request to clarify the classification and measurement of share-based payment transactions for which the manner of settlement is contingent on either:

- a future event that is outside the control of both the entity and the counterparty; or
- a future event that is within the control of the counterparty.

The IFRIC noted that paragraphs 34-43 of IFRS 2 provide guidance only on share-based payment transactions in which the terms of the arrangement provide the counterparty or the entity with a choice of settlement.

The IFRIC noted that IFRS 2 does not provide guidance on share-based payment transactions for which the manner of settlement is contingent on a future event that is outside the control of both the entity and the counterparty. The IFRIC noted that many other issues have been raised concerning the classification and measurement of share-based payments as cash-settled or equity-settled. The IFRIC therefore noted that it would be more appropriate for these issues to be considered collectively as part of a post-implementation review of IFRS 2.

Therefore, the IFRIC decided not to add these issues to its agenda and recommended that those issues be dealt with by the IASB in a post-implementation review of IFRS 2.

IFRS 4 ***Insurance Contracts*** and IAS 32 ***Financial Instruments: Presentation*** - Scope issue for REITs

In some jurisdictions, a Real Estate Investment Trust (REIT) is a tax or regulatory designation used for an entity investing in real estate that meets certain criteria, for example to attain preferential income tax status. In some of these cases, the contractual terms of the ownership units of such REITs require it to distribute 90 per cent of the Total Distributable Income (TDI) to the investors. The remaining 10 per cent of TDI may be distributed at the discretion of management. The IFRIC received a request to provide guidance on whether the discretion to distribute the remaining 10 per cent of TDI met the definition of a Discretionary Participation Feature (DPF) as defined in IFRS 4. If the DPF definition is met, IFRS 4 permits the ownership units to be classified as a liability, rather than assessing the instrument for financial liability and equity components in accordance with IAS 32.

The IFRIC noted that the objective of IFRS 4 is to specify the financial reporting for insurance contracts. The IFRIC noted that the definition of DPF in Appendix A of IFRS 4 requires, among other things, that the instrument provides the holder with guaranteed benefits and that the DPF benefits are additional to those guaranteed benefits. Furthermore, the IFRIC noted that there must be guaranteed benefits to the holder for the definition to be met and that such guaranteed benefits are typically those present in insurance activities. The IFRIC noted that providing guidance on this issue would be in the nature of application guidance, rather than interpretative guidance. Consequently, the IFRIC decided not to add the issue to its agenda.

IAS 18 ***Revenue*** - Receipt of a dividend of equity instruments

The IFRIC received a request for guidance on the recognition as revenue of a dividend in the financial statements of an investor when the dividend is in the form of the investee's own equity instruments.

The IFRIC noted that current IFRSs provide guidance on when revenue arising from dividends shall be recognised. The IFRIC noted that when all ordinary shareholders are issued a dividend of an investee's own equity instruments on a pro-rata basis there is no change in the financial position or economic interest of any of the investors. In this situation, in accordance with paragraph 29(a) of IAS 18, the dividend is not recognised as revenue because it is not probable that there is an economic benefit associated with the transaction that will flow to the investor.

The IFRIC concluded that any guidance it could provide would be in the form of application guidance. Consequently, the IFRIC decided not to add this issue to its agenda.

IAS 27 ***Consolidated and Separate Financial Statements*** - Combined financial statements and redefining the reporting entity

The IFRIC received a request for guidance on whether a reporting entity may, in accordance with IFRSs, present financial statements that include a selection of entities that are under common control, rather than being restricted to a parent/subsidiary relationship as defined by IAS 27.

The IFRIC noted that the ability to include entities within a set of IFRS financial statements depends on the interpretation of 'reporting entity' in the context of common control. The IFRIC noted that in December 2007 the Board added a project to its research agenda to examine the definition of common control and the methods of accounting for business combinations under common control in the acquirer's consolidated and separate financial statements. The IFRIC also noted that describing the reporting entity is the objective of Phase D of the Board's *Conceptual Framework* project.

The IFRIC also received a request for guidance on whether a reporting entity may, in accordance with IFRSs, be redefined to exclude from comparative periods entities/businesses that have been carved-out of a group. The IFRIC noted that the Board's common control project referred to above will also consider the accounting for demergers, such as the spin-off of a subsidiary or business. Consequently, the IFRIC decided not to add these issues to its agenda.

### IAS 27 ***Consolidated and Separate Financial Statements*** - Presentation of comparatives when applying the 'pooling of interests' method

The IFRIC received a request for guidance on the presentation of comparatives when applying the 'pooling of interests' method for business combinations between entities under common control when preparing financial statements in accordance with IFRS.

The IFRIC noted that IFRS 3 Business Combinations (revised 2008) excludes from its scope 'a combination of entities or businesses under common control'. The IFRIC noted that resolving the issue would require interpreting the interaction of multiple IFRSs. The IFRIC also noted that in December 2007 the Board added a project to its research agenda to examine the definition of common control and the methods of accounting for business combinations under common control in the acquirer's consolidated and separate financial statements. Consequently, the IFRIC decided not to add this issue to its agenda.

### IAS 32 ***Financial Instruments: Presentation*** - Application of the 'fixed for fixed' condition

The IFRIC received requests for guidance on the application of paragraph 22 of IAS 32 which states that 'except as stated in paragraph 22A, a contract that will be settled by the entity (receiving or) delivering a fixed number of its own equity instruments in exchange for a fixed amount of cash or another financial asset is an equity instrument' (often referred to as the 'fixed-for-fixed' condition).

The IFRIC identified that diversity may exist in practice in the application of the fixed-for-fixed condition to other situations in addition to the specific situations identified in the requests.

The IFRIC noted that the Board is currently undertaking a project to improve and simplify the financial reporting requirements for financial instruments with characteristics of equity. A key objective of this project is to develop a better distinction between equity and non-equity instruments. This includes consideration of the current fixed-for-fixed condition in IAS 32.

Consequently, the IFRIC concluded that the Board's current project on *Financial Instruments with Characteristics of Equity* is expected to address issues relating to the fixed-for-fixed condition on a timely basis. Consequently, the IFRIC decided not to add this issue to its agenda.

### IAS 38 ***Intangible Assets*** - Amortisation method

The IFRIC received requests for guidance on the meaning of 'consumption of economic benefits' when determining the appropriate amortisation method for an intangible asset with a finite useful life. The methods considered in the submissions are the straight-line method and the unit of production method (including a revenue-based unit of production method).

The IFRIC noted that paragraph 98 of IAS 38 states that 'the method used is based on the expected pattern of consumption of the expected future economic benefits embodied in the asset...' Some members of the IFRIC believed that an interpretation could assist in reducing diversity in the implementation of this principle, while others considered that any guidance would be in the nature of application guidance. The IFRIC noted that the determination of the amortisation method is therefore a matter of judgement. In addition, in accordance with paragraph 122 of IAS 1 *Presentation of Financial Statements*, significant judgements made in determining the amortisation methods should be disclosed in the notes to the financial statements.

Given the diversity of views, the IFRIC concluded that it would not be able to reach a consensus on the issue on a timely basis. Consequently, the IFRIC decided not to add the issue to its agenda.

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# Tentative agenda decisions

*The IFRIC reviewed the following matters and tentatively decided that they should not be added to the IFRIC agenda. These tentative decisions, including recommended reasons for not adding the items to the IFRIC agenda, will be reconsidered at the IFRIC meeting in March 2010. Constituents who disagree with the proposed reasons, or believe that the explanations may contribute to divergent practices, are encouraged to communicate those concerns by 13 February 2010 by email to:* ***ifric@iasb.org****. Communications will be placed on the public record unless the writer requests confidentiality, supported by good reasons, such as commercial confidence.*

### IAS 21 ***The Effects of Changes in Foreign Exchange Rates*** - Determination of functional currency of an investment holding company

The IFRIC received a request for guidance on whether the underlying economic environment of subsidiaries should be considered in determining, in its separate financial statements, the functional currency of an investment holding company.

IAS 21 paragraphs 9 - 11 provide factors to be considered in determining the functional currency of an entity. Paragraph 12 states that when the 'indicators are mixed and the functional currency is not obvious, management uses its judgement to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and conditions'.

Consequently, how an entity applies IAS 21 for the purpose of determining its functional currency - whether it is an investment holding company or any other type of entity - requires the exercise of judgement. IAS 1 *Presentation of Financial Statements* requires disclosure of significant accounting policies and judgements that are relevant to an understanding of the financial statements.

The IFRIC noted that any guidance it could provide would be in the nature of application guidance rather than an interpretation. Consequently, the IFRIC [decided] not to add the issue to its agenda.

### IAS 32 ***Financial Instruments: Presentation*** - Shareholder discretion

The IFRIC received a request for guidance on whether a financial instrument in the form of a preference share that includes a contractual obligation to deliver cash is a financial liability or equity, if the payment is at the ultimate discretion of the issuer's shareholders.

The IFRIC noted that paragraph AG26 of IAS 32 identifies that when distributions to holders of preference shares are at the discretion of the issuer, the shares are equity instruments.

The IFRIC identified that diversity may exist in practice in assessing whether an entity has an unconditional right to avoid delivering cash if the contractual obligation is at the ultimate discretion of the issuer's shareholders, and consequently whether a financial instrument should be classified as a financial liability or equity.

The IFRIC noted that the Board is currently undertaking a project to improve and simplify the financial reporting requirements for financial instruments with characteristics of equity. The main objectives of this project are to develop a better distinction between equity and non-equity instruments and converge IFRSs and US GAAP.

Consequently, the IFRIC concluded that the Board's current project on *Financial Instruments with Characteristics of Equity* is expected to address the distinction between equity and non-equity instruments on a timely basis. The IFRIC therefore [decided] not to add this issue to its agenda.

### IAS 36 ***Impairment of Assets*** - Interaction with transition requirements of IFRS 8

The IFRIC received a request for guidance on the transition requirements in IFRS 8 Operating Segments and its interaction with IAS 36 *Impairment of Assets*.

The IASB made a consequential amendment to IAS 36 when it issued IFRS 8 in November 2006. The consequential amendment replaced the reference to 'segments' (as determined in accordance with IAS 14 *Reporting Segments*) to 'operating segments' (as determined in accordance with IFRS 8). In particular, paragraph 80(b) of IAS 36 was amended to refer to IFRS 8 when setting the limit for the aggregation of cash-generating units when testing for goodwill impairment. Previously, the limit had been set by reference to segments identified by IAS 14. The IFRIC noted that when entities test goodwill for impairment in the first year of adoption of IFRS 8, some entities may need to recognise an impairment loss for goodwill, at least in part because of these changes in the segment definitions.

The question asked of the IFRIC is whether any incremental goodwill impairment loss (that would have been recognised in a prior period if cash-generating units had been grouped by reference to IFRS 8) determined as a result of retrospective application of the change from IAS 14 to IFRS 8 should be presented as a prior period adjustment or a current period event.

The IFRIC noted that IFRS 8 is effective for annual periods beginning on or after 1 January 2009 and is therefore applicable for entities with annual periods ending 31 December 2009 and thereafter. Based on the required due process procedures included in the IFRIC *Due Process Handbook*, the IFRIC would not be able to provide guidance on a timely basis. Consequently, the IFRIC [decided] not to add the issue to its agenda.

### IAS 39 ***Financial Instruments: Recognition and Measurement*** - Unit of account for forward contracts with volumetric optionality

The IFRIC received a request to add an item to its agenda on providing guidance on whether a contract that:

(a) obliges an entity to deliver (sell) at a fixed price a fixed number of units of a non-financial item that is readily convertible to cash; and

(b) provides the counterparty with the option to purchase, also at a fixed price, a fixed number of additional units of the same item

can be assessed as two separate contracts for the purpose of applying paragraphs 5 7 of IAS 39 *Financial Instruments: Recognition and Measurement*.

Although the IFRIC recognised that diversity exists in practice, it noted that the Board has accelerated its project to develop a replacement for IAS 39 and expects to issue a comprehensive replacement standard by the end of 2010. The Board will consider the scope of IAS 39, including the guidance about contracts to buy or sell non-financial items in paragraphs 5 - 7 of IAS 39, as part of the replacement for that standard. Consequently, the IFRIC [decided] not to add this issue to its agenda.

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# Annual improvements

*The IFRIC assists the IASB in its Annual Improvements project by reviewing proposed improvements to IFRSs and making recommendations to the Board. Specifically, the IFRIC involvement includes reviewing and deliberating issues for their inclusion in future exposure drafts of proposed Improvements to IFRSs and deliberating the comments received on the exposure drafts. When the IFRIC has reached consensus on an issue included in the Annual Improvements project, the recommendation (including finalisation of the proposed amendment or removal from the project) will be presented to the Board for ratification, in a public meeting, before being finalised. Approved Improvements to IFRSs (including exposure drafts and final standards) are issued by the Board.*

At the meeting in January 2010, the IFRIC deliberated the comments received on seven proposed amendments included in the exposure draft of proposed *Improvements to IFRSs* published in August 2009. The IFRIC also deliberated the two remaining proposed amendments included in the exposure draft of proposed *Improvements to IFRSs* published in August 2008.

## Confirmed proposed amendments.

The IFRIC confirmed six of the proposed amendments, subject to its final review of drafting changes, and submitted the proposed amendments to the Board for ratification at a future Board meeting. Subject to ratification, the Board will include the amendments in the *Improvements to IFRSs* expected to be issued in April 2010. The six confirmed proposed amendments were:

### IFRS 1 ***First-time Adoption of International Financial Reporting Standards*** - Fair value or revaluation as deemed cost exemption - paragraph D8

The IFRIC confirmed the proposed amendment to extend the scope of the exemption in paragraph D8 to be applicable to events occurring after transition date, but before the end of the entity's first IFRS reporting period. As part of its deliberations on the comments received, the IFRIC decided to include minor modifications to the proposed amendment to specify how the event-driven revaluation is recognised and to clarify the effective date.

### IFRS 3 ***Business Combinations*** - Transition requirements for contingent consideration from a business combination that occurred before the effective date of the revised IFRS 3

The IFRIC confirmed the proposed amendment to clarify that for existing users of IFRSs the financial instruments standards (IFRS 7, IAS 32 and IAS 39) do not apply to contingent consideration arising from a business combination whose acquisition date preceded the application of IFRS 3 (revised 2008).

Having considered the comments received, the IFRIC decided to modify the proposed amendment to reproduce the IFRS 3 (issued 2004) requirements on accounting for contingent consideration within the transition section in IFRS 3 (revised 2008), after paragraph 65, and refer to this guidance in the transition sections of IFRS 7, IAS 32 and IAS 39. The IFRIC decided that this guidance shall be applied to all contingent consideration balances arising from acquisitions prior to the date the entity first applied IFRS 3 (revised 2008).

In addition, the IFRIC recommended that the Board consider, as part of its project to replace IAS 39, bringing together in one IFRS the measurement guidance for contingent consideration that is a financial instrument.

### IFRS 3 ***Business Combinations*** - Measurement of non-controlling interests

The IFRIC confirmed the proposed amendment to paragraph 19 of IFRS 3 (revised 2008) to clarify that the choice for measuring the non-controlling interest in the acquiree applies only to 'components of non-controlling interests that are present ownership instruments and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation'. Other present ownership instruments that are classified as non-controlling interests should be measured 'at fair value, unless another measurement basis is required by IFRSs'.

The IFRIC also asked the staff to prepare examples to be included in the confirmed proposed amendment that would illustrate the application of the requirement.

### IFRS 7 ***Financial Instruments: Disclosures*** - Clarifications of disclosures

The IFRIC confirmed the proposed amendment to IFRS 7 that clarifies and amends the qualitative, quantitative and credit risk disclosures included in paragraphs 33-38. As part of its deliberations on the comments received, the IFRIC decided to include minor modifications to the proposed amendment.

These modifications remove the proposed paragraph 33A and add a paragraph to emphasise the interaction between qualitative and quantitative disclosures so as to contribute to disclosure of information in a way that better enables users to evaluate an entity's exposure.

### IAS 28 ***Investments in Associates*** - Partial use of fair value for measurement of associates

The IFRIC confirmed the proposed amendment to clarify that different measurement bases can be applied to portions of an investment in an associate when part of the investment is designated at initial recognition as at fair value through profit or loss in accordance with the scope exception in paragraph 1 of IAS 28.

The IFRIC confirmed that an entity first determines whether it has significant influence over an associate in accordance with paragraphs 6-10 of IAS 28. Next the entity measures, at fair value through profit or loss, the portion of the investment in the associate to which the scope exception applies. The remaining investment in the associate is accounted for in accordance with IAS 28.

In addition, the IFRIC recommended that the Board consider including a similar amendment for accounting for interests in joint ventures, possibly by inclusion in the forthcoming IFRS on joint arrangements.

### IAS 34 ***Interim Financial Reporting*** - Significant events and transactions

The IFRIC confirmed the proposed amendment to emphasise the existing disclosure principles in IAS 34 and to add further guidance to illustrate how to apply these principles. As part of its deliberations on the comments received, the IFRIC decided to include minor modifications to the proposed amendment including an explanation in the Basis for Conclusions of the rationale for the removal of paragraph 18.

### Proposed amendments recommended for removal, without finalisation, from the Annual Improvements project

The IFRIC confirmed that three of the proposed amendments should not be finalised. The IFRIC also confirmed that these three proposed amendments should be formally removed from the *Annual Improvements* project. In reaching this conclusion, the IFRIC noted that the Board has an accelerated project to replace IAS 39. The IFRIC believes these issues should be reconsidered taking into account the broad IAS 39 replacement project and not considered on a piecemeal basis. The three proposed amendments were included in the exposure drafts of proposed *Improvements to IFRSs* published in the periods referenced below:

- IAS 39 ***Financial Instruments: Recognition and Measurement*** - Bifurcation of embedded foreign currency derivative (published August 2008)
- IAS 39 ***Financial Instruments: Recognition and Measurement*** - Application of the fair value option (published August 2008)
- IAS 27 ***Consolidated and Separate Financial Statements*** - Impairment of investments in subsidiaries, jointly controlled entities and associates in the separate financial statements of the investor (published August 2009)

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## IFRIC work in progress

### IFRS 1 ***First-time Adoption of International Financial Reporting Standards*** - Accounting for costs included in self-constructed assets on transition

The IFRIC received two requests concerning the application of IFRSs for an entity that has capitalised certain costs as part of self-constructed assets in accordance with a previous GAAP accounting policy. This previous GAAP accounting policy is also compliant with IFRSs. On transition to IFRSs, the entity elects to change this accounting policy. If this revised policy were applied to costs capitalised in accordance with previous GAAP at the date of transition to IFRSs, the carrying amount of self constructed assets (for example, construction contract assets and inventory) may be different.The requests sought clarification on whether IFRS 1 required the previous GAAP carrying amounts of these assets to be restated at transition date.

The IFRIC did not make any tentative decisions, but directed the staff to research the issue further.

### IFRIC outstanding issues update

The IFRIC reviewed a summary of outstanding issues. With the exception of four issues, all requests received and considered by the staff were discussed at this meeting. The remaining four issues are expected to be discussed at the March 2010 IFRIC meeting.

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## Future IFRIC meetings 2010

The IFRIC's meetings are expected to take place in London, UK as follows:

4 and 5 March

6 and 7 May

8 and 9 July

2 and 3 September

4 and 5 November

In addition to the meetings listed above, the IFRIC may hold meetings for a preliminary discussion of some staff papers. Attendance by IFRIC members at these meetings is voluntary and no decisions on technical issues will be made. If the IFRIC holds a preliminary meeting, it will normally take place on the Wednesday afternoon before the IFRIC meeting.

Meeting dates, tentative agendas and additional details about the next meeting will also be posted to the IASB website before the meeting. Instructions for submitting requests for Interpretations are given on the IASB website - click here.

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ISSN 1477-206X