IFRIC Update September 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 17 September 2019, and discussed:

Committee's tentative agenda decisions

- Training Costs to Fulfil a Contract (IFRS 15 *Revenue from Contracts with Customers*)—Agenda Paper 2
- Definition of a Lease—Shipping Contract (IFRS 16 *Leases*)—Agenda Paper 3
- Translating a Hyperinflationary Foreign Operation—Presenting Exchange Differences (IAS 21 *The Effects of Changes in Foreign Exchange Rates* and IAS 29 *Financial Reporting in Hyperinflationary Economies*)—Agenda Paper 4A
- Cumulative Exchange Differences before a Foreign Operation becomes Hyperinflationary (IAS 21 and IAS 29)—Agenda Paper 4B
- Presenting Comparative Amounts when a Foreign Operation first becomes Hyperinflationary (IAS 21 and IAS 29)—Agenda Paper 4C

Committee's agenda decisions

- Compensation for Delays or Cancellations (IFRS 15 *Revenue from Contracts with Customers*)—Agenda Paper 5
- Lessee's Incremental Borrowing Rate (IFRS 16 *Leases*)—Agenda Paper 8
- Fair Value Hedge of Foreign Currency Risk on Non-Financial Assets (IFRS 9 *Financial Instruments*)—Agenda Paper 9
- Presentation of Liabilities or Assets Related to Uncertain Tax Treatments (IAS 1 *Presentation of Financial Statements*)—Agenda Paper 10
- Disclosure of Changes in Liabilities Arising from Financing Activities (IAS 7 *Statement of Cash Flows*)—Agenda Paper 7
- Subsequent Expenditure on Biological Assets (IAS 41 *Agriculture*)—Agenda Paper 6

Other matters

- Committee Work in Progress—Agenda Paper 11

Related information

Next scheduled IFRS Interpretations Committee meeting:

- 26 November 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 25 November 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 25 November 2019; agenda papers analysing comments received will include analysis only of comments received by that date.

Training Costs to Fulfil a Contract (IFRS 15 *Revenue from Contracts with Customers*)—Agenda Paper 2

The Committee received a request about training costs incurred to fulfil a contract with a customer. In the fact pattern described in the request:

a. an entity enters into a contract with a customer that is within the scope of IFRS 15. The contract is for the supply of outsourced services.

b. to be able to provide the services to the customer, the entity incurs costs to train its employees (as described in paragraph 15 of IAS 38 *Intangible Assets*) so that they understand the customer's equipment and processes. Applying IFRS 15, the entity does not identify the training activities as a performance obligation.

c. the contract permits the entity to charge to the customer the costs of training (i) the entity's employees at the beginning of the contract, and (ii) new employees that the entity hires as a result of any expansion of the customer's operations.

The request asked whether the entity recognises the training costs as an asset or an expense when incurred.

Which IFRS Standard applies to the training costs?

Paragraph 95 of IFRS 15 requires an entity to recognise an asset from the costs incurred to fulfil a contract with a customer not within the scope of another IFRS Standard, only if those costs meet all three criteria specified in paragraph 95. Consequently, before assessing the criteria in paragraph 95, the entity first considers whether the training costs incurred to fulfil the contract are within the scope of another IFRS Standard.

Paragraph 5 of IAS 38 states that 'this Standard applies to, among other things, expenditure on advertising, training, start-up, research and development activities'. Accordingly, the Committee concluded that, in the fact pattern described in the request, the entity applies IAS 38 in accounting for the training costs incurred to fulfil the contract with the customer.

Application of IAS 38

Paragraph 69(b) of IAS 38 lists 'expenditure on training activities' as an example of expenditure that an entity recognises as an expense when incurred. Paragraph 15 of IAS 38 explains that 'an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset'.

In addition, in explaining the requirements in IFRS 15 regarding costs to fulfil a contract, paragraph BC307 of IFRS 15 states that 'if the other Standards preclude the recognition of any asset arising from a particular cost, an asset cannot then be recognised under IFRS 15'.

Accordingly, the Committee concluded that, in the fact pattern described in the request, the entity recognises as an expense when incurred the training costs to fulfil the contract with the customer.

The Committee concluded that the principles and requirements in IFRS 15 and IAS 38 provide an adequate basis for an entity to determine its accounting for training costs incurred to fulfil a contract with a customer. Consequently, the Committee [decided] not to add this matter to its standard-setting agenda.

Definition of a Lease—Shipping Contract (IFRS 16 *Leases*)—Agenda Paper 3

The Committee received a request about whether the customer has the right to direct the use of a ship throughout the five-year term of a particular contract. In the fact pattern described in the request:

a. there is an identified asset (the ship) applying paragraphs B13–B20 of IFRS 16.

b. the customer has the right to obtain substantially all the economic benefits from use of the ship throughout the five-year period of use applying paragraphs B21–B23 of IFRS 16.

c. many, but not all, of the relevant decisions about how and for what purpose the ship is used are predetermined in the contract. The customer has the right to make the remaining relevant decisions about how and for what purpose the ship is used throughout the period of use. Those decision-making rights are relevant because they affect the economic benefits to be derived from use of the ship.

d. the supplier operates and maintains the ship throughout the period of use.

The right to direct the use of an asset

Paragraph B24 of IFRS 16 specifies when a customer has the right to direct the use of an identified asset throughout the period of use. Paragraph B24(b) applies only when the relevant decisions about how and for what purpose the asset is used are predetermined. The Board noted in paragraph BC121 of IFRS 16 that 'it would expect decisions about how and for what purpose an asset is used to be predetermined in relatively few cases'.

The Committee observed that, in the fact pattern described in the request, because not all relevant decisions about how and for what purpose the ship is used are predetermined, the customer considers paragraph B24(a) of IFRS 16 in assessing whether it has the right to direct the use of the ship.

The right to direct how and for what purpose an asset is used

Paragraph B24(a) specifies that a customer has the right to direct the use of an identified asset throughout the period of use if it has 'the right to direct how and for what purpose the asset is used throughout the period of use (as described in paragraphs B25–B30)'.

For the customer to have the right to direct how and for what purpose the asset is used, within the scope of its right of use defined in the contract, the customer must be able to change how and for what purpose the asset is used throughout the period of use (paragraph B25). In assessing whether that is the case, 'an entity considers the decision-making rights that are most relevant to changing how and for what purpose the asset is used throughout the period of use. Decision-making rights are relevant when they affect the economic benefits to be derived from use' (paragraph B25).

Paragraph B26 includes examples of decision-making rights that, depending on the circumstances, grant the right to change how and for what purpose the asset is used. Rights limited to operating or maintaining the asset do not grant the right to change how and for what purpose an asset is used (paragraph B27).

The Committee observed that, in the fact pattern described in the request, the customer has the right to direct how and for what purpose the ship is used throughout the five-year period of use. This is because, within the scope of its right of use defined in the contract, the customer can change how and for what purpose the ship is used. The predetermination in the contract of many of the relevant decisions about how and for what purpose the ship is used defines the scope of the customer's right of use. Within that scope, the customer has the right to make all the relevant decisions about how and for what purpose the ship is used that can be made.

The Committee also observed that, although the operation and maintenance of the ship are essential to its efficient use, the supplier's decisions in this regard do not give it the right to direct how and for what purpose the ship is used.

The Committee concluded that, in the fact pattern described in the request, the customer has the right to direct the use of the ship throughout the five-year period of use and, consequently, the contract contains a lease.

The Committee concluded that the principles and requirements in IFRS 16 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.

Translating a Hyperinflationary Foreign Operation—Presenting Exchange Differences (IAS 21 *The Effects of Changes in Foreign Exchange Rates* and IAS 29 *Financial Reporting in Hyperinflationary Economies*)—Agenda Paper 4A

The Committee received a request about the application of IAS 21 and IAS 29. In the fact pattern described in the request, the entity:

a. has a presentation currency that is not the currency of a hyperinflationary economy as defined in IAS 29;

b. has a foreign operation with a functional currency that is the currency of a hyperinflationary economy as defined in IAS 29 (hyperinflationary foreign operation); and

c. translates the results and financial position of the hyperinflationary foreign operation into its presentation currency in preparing its consolidated financial statements.

Paragraph 43 of IAS 21 requires an entity to restate the results and financial position of a hyperinflationary foreign operation applying IAS 29 before applying the translation method set out in paragraph 42 of IAS 21 (restate/translate approach). The application of the restate/translate approach may result in a change to the entity's net investment in the hyperinflationary foreign operation. This change would include two effects:

a. a restatement effect resulting from restating the entity's interest in the net assets of the hyperinflationary foreign operation as required by IAS 29; and

b. a translation effect resulting from translating the entity's interest in the net assets of the hyperinflationary foreign operation (excluding the effect of any restatement required by IAS 29) at a closing rate that differs from the previous closing rate.

To illustrate using a simple example, assume at the beginning of the reporting period an entity has a 100% interest in a hyperinflationary foreign operation that has a non-monetary asset of 1,000 in local currency (LC), no other assets and no liabilities. Therefore, the foreign operation has net assets of LC1,000. The change in the general price index of the hyperinflationary economy during the reporting period is 200%. The entity could, for example, calculate:

a. the restatement effect as (LC1,000 * 200% - LC1,000) * closing exchange rate. This calculation reflects the entity's interest in the net assets of the hyperinflationary foreign operation of LC1,000, restated applying IAS 29, and reported in the entity's presentation currency; and

b. the translation effect as (LC1,000 * closing exchange rate) – (LC1,000 * opening exchange rate). This calculation reflects the entity's interest in the net assets of the hyperinflationary foreign operation of LC1,000 (excluding the effect of any restatement required by IAS 29) multiplied by the difference between the opening and closing exchange rates.

The request asked how the entity presents the restatement and translation effects in its statement of financial position.

Do the restatement and translation effects meet the definition of an exchange difference?

Paragraph 8 of IAS 21 defines an exchange difference as the difference 'resulting from translating a given number of units of one currency into another currency at different exchange rates'. The Committee concluded that, in the fact pattern described in the request, either the translation effect alone meets the definition of an exchange difference, or the combination of the restatement and translation effects meets that definition.

How does an entity present any exchange difference arising from translating a hyperinflationary foreign operation?

The Committee observed that all requirements in IAS 21 that specify the recognition (or presentation) of exchange differences require an entity to recognise (or present) exchange differences in profit or loss or other comprehensive income (OCI).

IAS 21 requires the recognition of exchange differences in profit or loss or OCI—with no reference to equity—because exchange differences meet the definition of income or expenses. Accordingly, the Committee concluded that an entity does not recognise exchange differences directly in equity.

Paragraph 41 of IAS 21 specifies why paragraph 39(c) of IAS 21 requires an entity whose functional currency is not the currency of a hyperinflationary economy to present in OCI—and not in profit or loss—any exchange difference arising when the entity's results and financial position are translated into a non-hyperinflationary presentation currency. The Committee observed that this explanation also applies if the functional currency is hyperinflationary. Accordingly, the Committee concluded that an entity presents in OCI any exchange difference resulting from the translation of a hyperinflationary foreign operation.

Applying the requirements in IFRS Standards to the restatement and translation effects

The Committee concluded that, in the fact pattern described in the request, the entity presents:

a. the restatement and translation effects in OCI, if the entity considers that the combination of those two effects meets the definition of an exchange difference in IAS 21; or

b. the translation effect in OCI, if the entity considers that only this translation effect meets the definition of an exchange difference in IAS 21. In this case, consistent with the requirements in paragraph 25 of IAS 29, the entity would present the restatement effect in equity.

In the light of its analysis, the Committee considered whether to add a project on the presentation of exchange differences resulting from the restatement and translation of hyperinflationary foreign operations to its standard-setting agenda. The Committee has not [yet] obtained evidence that a project would result in an improvement in financial reporting that would be sufficient to outweigh the costs.

Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Cumulative Exchange Differences before a Foreign Operation becomes Hyperinflationary (IAS 21 *The Effects of Changes in Foreign Exchange Rates* and IAS 29 *Financial Reporting in Hyperinflationary Economies*)—Agenda Paper 4B

The Committee received a request about the application of IAS 21 and IAS 29. In the fact pattern described in the request, the entity:

a. has a presentation currency that is not the currency of a hyperinflationary economy as defined in IAS 29;

b. has a foreign operation with a functional currency that is the currency of a hyperinflationary economy as defined in IAS 29 (hyperinflationary foreign operation); and

c. translates the results and financial position of the hyperinflationary foreign operation into its presentation currency in preparing its consolidated financial statements.

Before the foreign operation becomes hyperinflationary, IAS 21 requires an entity to:

a. present in other comprehensive income (OCI) any exchanges differences resulting from translating the results and financial position of that non-hyperinflationary foreign operation; and

b. present in a separate component of equity the cumulative amount of those exchange differences (cumulative pre-hyperinflation exchange differences).

The request asked whether, at the beginning of the period during which the foreign operation becomes hyperinflationary, the entity reclassifies within equity the cumulative pre-hyperinflation exchange differences—that is, whether the entity transfers the cumulative pre-hyperinflation exchange differences to a component of equity that is not subsequently reclassified to profit or loss.

The Committee observed that paragraph 41 of IAS 21 requires the entity to present the cumulative pre-hyperinflation exchange differences in a separate component of equity ‘until disposal of the foreign operation’. Furthermore, paragraph 48 of IAS 21 requires the entity to reclassify the cumulative pre-hyperinflation exchange differences from equity to profit or loss (as a reclassification adjustment) on disposal of the foreign operation.

Accordingly, the Committee concluded that, in the fact pattern described in the request, the entity retains the cumulative pre-hyperinflation exchange differences as a separate component of equity (to which paragraph 48 of IAS 21 applies) until disposal of the foreign operation. The entity does not reclassify within equity the cumulative pre-hyperinflation exchange differences when the foreign operation becomes hyperinflationary.

The Committee concluded that the principles and requirements in IAS 21 provide an adequate basis for an entity to determine how to present the cumulative pre-hyperinflation exchange differences when a foreign operation becomes hyperinflationary. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Presenting Comparative Amounts when a Foreign Operation first becomes Hyperinflationary (IAS 21 *The Effects of Changes in Foreign Exchange Rates* and IAS 29 *Financial Reporting in Hyperinflationary Economies*)—Agenda Paper 4C

The Committee received a request about the application of IAS 21 and IAS 29. In the fact pattern described in the request, the entity:

a. has a presentation currency that is not the currency of a hyperinflationary economy as defined in IAS 29;

b. has a foreign operation whose functional currency is the currency of a hyperinflationary economy as defined in IAS 29 (hyperinflationary foreign operation); and

c. translates the results and financial position of the hyperinflationary foreign operation into its presentation currency in preparing its consolidated financial statements.

The request asked whether the entity restates comparative amounts presented for the foreign operation in:

a. its annual financial statements for the period in which the foreign operation becomes hyperinflationary; and

b. its interim financial statements in the year after the foreign operation becomes hyperinflationary, if the foreign operation was not hyperinflationary during the comparative interim period.

On the basis of responses to outreach and additional research performed, the Committee observed little, if any, diversity in the application of IAS 21 with respect to the questions in the request—in applying paragraph 42(b) of IAS 21, entities generally do not restate comparative amounts in their interim or annual financial statements in the situations described above. Therefore, the Committee has not [yet] obtained evidence that the matter has widespread effect.

Consequently, the Committee [decided] not to add this 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.

Compensation for Delays or Cancellations (IFRS 15 *Revenue from Contracts with Customers*)—Agenda Paper 5

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 forms part of the consideration to which the entity expects to be entitled in exchange for transferring the promised service to the customer;

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 give 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 8

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, it would be consistent with the Board's objective when developing the definition of incremental borrowing rate for a lessee to 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.

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

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, in some cases, 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 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 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 a) foreign currency risks, or b) 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 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 grounds 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 is unlikely to be managing and using hedging instruments to hedge risk exposures on the non-financial asset and, in that case, it cannot apply hedge accounting.

The Committee expects that an entity would manage and hedge exposure to foreign currency risk on the fair value of non-financial assets held for consumption only in very limited circumstances—in such circumstances, an entity would use hedging instruments to hedge only foreign currency risk exposure that it expects will affect profit or loss. This may be the case, for example, if (a) the entity expects to sell the non-financial asset (eg an item of property, plant and equipment) part-way through its economic life; (b) the expected residual value of the asset at the date of expected sale is significant; and (c) the entity manages and uses hedging instruments to hedge the foreign currency risk exposure only on the residual value of the asset.

Furthermore, the Committee observed that risk management activities that aim only to reduce foreign exchange volatility arising from translating a financial liability denominated in a foreign currency applying IAS 21 are inconsistent with the designation of foreign exchange risk on a non-financial asset as the hedged item in a fair value hedge accounting relationship. In such circumstances, the entity is managing the foreign currency risk exposure arising on the financial liability, rather than managing the risk exposure arising on the non-financial asset.

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 the hedged item and hedging instrument, 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 principles and 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.

Presentation of Liabilities or Assets Related to Uncertain Tax Treatments (IAS 1 *Presentation of Financial Statements*)—Agenda Paper 10

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 request 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, can present such liabilities 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 principles and 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 7

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 the objective in paragraph 44A, 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.

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

Paragraph 44D of IAS 7 states that 'one 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 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 for the entity to identify its 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.

c. paragraph 44D 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 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 to meet the objective in paragraph 44A. 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 an entity 'shall not reduce the understandability of its financial statements…by aggregating material items that have different natures or functions'. Accordingly, 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.

Accordingly, the Committee concluded that the principles and 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 6

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.

IAS 41 does not specify the accounting for subsequent expenditure for biological assets measured at fair value less costs to sell. Paragraph B62 of the Basis for Conclusions on IAS 41 explains that '…the [IASC] 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. The Committee observed that capitalising subsequent expenditure or recognising it as an expense has no effect on the fair value 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. In assessing how to present such subsequent expenditure in the statement of profit or loss, an entity would apply the requirements in paragraphs 81–105 of IAS 1 *Presentation of Financial Statements*. In particular, the Committee observed that the entity would:

a. applying paragraph 85, 'present additional line items (including by disaggregating the line items listed in paragraph 82), headings and subtotals in the statement(s) presenting profit or loss and other comprehensive income when such presentation is relevant to an understanding of the entity's financial performance'; and

b. applying paragraph 99, present in the statement(s) presenting profit or loss and other comprehensive income or in the notes an analysis of expenses recognised in profit or loss using a classification based on either their nature or their function within the entity, whichever provides information that is reliable and more relevant.

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 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 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.

Other matters

Committee Work in Progress—Agenda Paper 11

The Committee received a report that provides an update on the current status of matters not discussed at its meeting in September 2019.