

October 2011

Summary of EFRAG meetings held in September - October 2011

On 26 September 2011, EFRAG held a meeting by public conference call to discuss its comment letters on:

- IASB Exposure Draft *Investment Entities*
- IFRS Interpretations Committee's tentative agenda decision on IAS 12 *Income Taxes – Rebuttable presumption to determine the manner of recovery*.

From 12 to 14 October 2011, EFRAG held its monthly meeting. The first day of the meeting was held together with the European national standard setters in EFRAG's Consultative Forum of Standard Setters (CFSS). The following topics were discussed during the monthly meeting:

- Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income*
- IAS 19 *Employee Benefits* (as amended in 2011)
- IFRS 13 *Fair Value Measurement*
- IASB's new standards related to *Consolidation* project – IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities*; IAS 27 *Separate Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (as amended in 2011)
- Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets*
- IASB Exposure Draft *Improvements to IFRSs 2009 – 2011*
- IASB Project *Financial Instruments*
- IASB Project *Revenue Recognition*
- IASB Draft Q&As on IFRS for SMEs
- IASB Agenda Consultation
- EFRAG Proactive Project *Income Tax*
- EFRAG Proactive Project *Disclosure Framework for the Notes to the Financial Statements*
- EFRAG Proactive Project *Considering the Effects of Accounting Standards*
- Developments affecting the implementation of IFRS in the United States.

Highlights

Endorsement Advice

EFRAG finalised its endorsement advice to the European Commission on the Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income* and IAS 19 *Employee Benefits* (as amended in 2011) (page 2 and 3 respectively).

Comment letters

EFRAG finalised its comment letter to the IFRS Interpretations Committee in response to the tentative agenda decision on IAS 12 *Income Tax – Rebuttable presumption to determine the manner of recovery*. EFRAG believes that the wording for rejection is in effect an interpretation. In EFRAG’s view, rejection notices should not be written as though they were authoritative guidance and should not result in a change in accounting practice (page 4).

EFRAG invited comments on its draft comment letters to the IASB in relation to the following:

- Exposure Draft *Investment Entities* – EFRAG broadly welcomes the proposal, but emphasises that the parent of an investment entity should be permitted to retain the fair value accounting that is applied by its investment entity subsidiary to controlled entities. EFRAG also encourages the IASB to carry out an impact assessment to better understand the practical implications of any amendments to IAS 28 *Investments in Associates and Joint Ventures*. The comment deadline is 27 December 2011 (page 2).
- Draft Q&As on IFRS for SMEs (third batch) – EFRAG recommends not issuing any of the Q&As because they do not focus on a limited number of pervasive issues as they should according to the terms of reference and operating procedures for the SME Implementation Group. The comment deadline is 18 November 2011 (page 6).

IASB Exposure Draft *Investment Entities*

During a meeting held by a public conference call on 26 September 2011, EFRAG finalised its draft comment letter in response to the IASB Exposure Draft *Investment Entities* (the ED), which was issued in August 2011. The ED provides criteria for and guidance on determining whether an entity is an investment entity. Under the proposals in the ED, investment entities measure their investments in controlled investees at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments*.

Whilst EFRAG broadly welcomed the proposal in the ED, it emphasised in the draft comment letter that the parent of an investment entity should be permitted to retain the fair value accounting applied by its investment entity subsidiary to controlled entities. EFRAG also encouraged the IASB to carry out an impact assessment to understand better the practical implications of any amendments to IAS 28 *Investments in Associates and Joint Ventures*.

The draft comment letter invites constituents to comment on whether the criteria for identifying investments entities are appropriate and whether the exception from the consolidation requirement should be applied at an entity level or at the level of individual investments. The draft comment letter is available on EFRAG’s website. The comment deadline is 27 December 2011.

Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income*

In July 2011, EFRAG issued an Invitation to Comment on its draft endorsement advice and a draft Effect Study Report in respect of the Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income (the Amendments)*, which was issued by the IASB in June 2011. The Amendments require separate presentation of items of other comprehensive income that are reclassified subsequently to profit or loss (recyclable) and those that are not reclassified to profit or loss (non-recyclable). If items of other comprehensive income are presented before tax, then income tax is allocated to each respective group. Based on the comments

received, EFRAG agreed to issue to the European Commission both the positive endorsement advice and the Effect Study Report.

IAS 19 *Employee Benefits* (as amended in 2011)

In July 2011, EFRAG issued an Invitation to Comment on its draft endorsement advice and a draft Effect Study Report in respect of a revised version of IAS 19 *Employee Benefits* (IAS 19 (2011)), which was issued by the IASB in June 2011. IAS 19 (2011) eliminates the ‘corridor approach’ in accounting for actuarial gains and losses; requires disaggregating pension costs into various components (which are subject to different accounting treatment); amends guidance on termination benefits; and enhances disclosures. Based on the comments received, EFRAG agreed to issue to the European Commission both the positive endorsement advice and the Effect Study Report.

IFRS 13 *Fair Value Measurement*

EFRAG discussed the initial assessment of IFRS 13 against the technical criteria for its endorsement in the EU. EFRAG focused on the impact of the new fair value measurement guidance on the quality of information about assets, liabilities and own equity instruments that are subject to fair value measurement or disclosure requirements. In particular, EFRAG considered the impact of defining the fair value as an exit price, the new concepts of the principal market and the highest and best use (for non-financial assets), and more comprehensive disclosures.

EFRAG will continue its initial assessment of IFRS 13 at the November 2011 meeting.

IASB’s new standards related to *Consolidation* project

During the session held together with the European national standard setters, EFRAG and CFSS members were updated on the status of the field-testing that EFRAG is conducting in cooperation with participating European national standard setters on the recently issued standards: IFRS 10, IFRS 11, and IFRS 12. The feedback received during the field-testing will be considered by EFRAG in its initial assessment of the standards against the technical criteria for the endorsement in the EU.

During its monthly meeting, EFRAG considered IAS 27 and IAS 28 (as amended in 2011) in view of its initial assessment of the amended standards against the technical criteria for the endorsement in the EU. EFRAG has tentatively decided that the invitation to comment on the EFRAG’s initial assessments for all the new standards related to *Consolidation* and *Joint Venture* projects (i.e., IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28 (as amended in 2011)) will be issued at the same time to reflect their interrelations.

IFRS Interpretations Committee’s tentative agenda decision on IAS 12 *Income Taxes - Rebuttable presumption to determine the manner of recovery*

EFRAG finalised its comment letter to the IFRS Interpretations Committee in response to the tentative agenda decision on IAS 12 *Income Tax – Rebuttable presumption to determine the manner of recovery*.

In December 2010 the IASB published Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets* (the Amendments). The Amendments introduce a rebuttable presumption that the carrying amount of the investment property will be recovered through sale in determining deferred taxes on investment property measured at fair value under IAS 40 *Investment Property*.

Paragraph 51C of IAS 12 (as amended) explains that the rebuttable presumption is rebutted if the investment property is depreciable and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale. If the presumption is rebutted, the requirements of paragraphs 51 and 51A shall be followed.

In September 2011, the IFRS Interpretations Committee received a request to clarify whether that presumption can be rebutted in cases other than the case described in paragraph 51C of IAS 12 (as amended). The IFRS Interpretations Committee decided not to add this item to its agenda and noted that in its view paragraph 51C of IAS 12 (as amended) is clear and that diversity in practice on the rebuttal of the presumption should not emerge. However, it also observed that, if the presumption is rebutted, the resulting deferred tax should reflect recovery of the carrying amount entirely through use, rather than be based on any dual purpose analysis.

In its comment letter to the IFRS Interpretations Committee EFRAG stated that the wording for rejection was in effect an interpretation. In EFRAG's view, rejection notices should not be written as though they were authoritative guidance and should not result in a change in accounting practice. The final decision to be made by the IFRS Interpretations Committee would be considered by EFRAG in developing its initial assessment of the Amendments against the technical criteria for their endorsement in the EU. The comment letter is available on EFRAG's website.

Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets*

As outlined in the preceding article, in December 2010, the IASB published Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets* (the Amendments). The Amendments introduce an exception to the measurement principles in IAS 12 to provide a practical solution for those cases when it is difficult or subjective to determine the manner, in which an entity expects to recover the carrying amount of investment property measured at fair value under IAS 40 *Investment Property*.

EFRAG discussed a revised draft of its initial assessments of the Amendments against the technical criteria for their endorsement in the EU and the initial analysis of their costs and benefits. When EFRAG first discussed the Amendments, some members expressed a concern about the potential loss of relevant information in circumstances, in which entities had sufficient evidence to rebut the presumption and could apply the measurement principles in IAS 12 but were "forced" to measure deferred tax using the tax rate on sale. Following an ensuing debate, EFRAG agreed that the overall effect of the Amendments on financial reporting could not be significant because the scope of the Amendments was restricted. The Invitation to Comment on the draft endorsement advice and a draft Effect Study Report at EFRAG's meeting in November.

IASB Exposure Draft *Improvements to IFRSs 2009 - 2011*

EFRAG discussed comments received in response to its draft comment letter on the IASB Exposure Draft *Improvements to IFRSs 2009-2011* (the ED). The ED proposes the following amendments to standards:

- IFRS 1 *First-time Adoption of International Financial Reporting Standards* – Repeated application of IFRS 1. Borrowing costs relating to qualifying assets for which the commencement date for capitalisation is before the date of transition to IFRSs.
- IAS 1 *Presentation of Financial Statements* – Clarification of requirements for comparative information. Consistency with the updated Conceptual Framework.
- IAS 16 *Property, Plant and Equipment* – Classification of servicing equipment.
- IAS 32 *Financial Instruments: Presentation* – Income tax consequences of distributions to holders of an equity instrument, and of transaction costs of an equity transaction.
- IAS 34 *Interim Financial Reporting* – Interim financial reporting and segment information for total assets.

In its draft comment letter, EFRAG supported most of the amendments proposed in the ED, however, suggested that the IASB should address the internal inconsistency in IAS 12 in relation to accounting for taxes on distributions to owners, rather than just amending IAS 32. The comments received from European constituents were generally consistent with EFRAG's position expressed in the draft comment letter, however, highlighted additional concerns about proposed amendments to IAS 1.

It was noted that changes to IFRSs proposed as a result of the revised *Conceptual Framework* were of the selective nature and suggested that the IASB should deal with such changes in a separate, fully reasoned, exposure draft. These concerns will be taken into account in finalising EFRAG's response to the IASB. EFRAG has also decided to recommend in its final comment letter that potential impacts of a change in the *Conceptual Framework* on existing standards be fully exposed at the same time as the proposed revised or a new chapter of the *Conceptual Framework*.

EFRAG will finalise its comment letter to the IASB on the ED at a public conference call scheduled for 26 October 2011.

IASB Project *Financial Instruments*

Members of the IASB Expert Advisory Panel made a presentation to EFRAG and CFSS on the new approach to impairment of financial assets considered by the IASB and the FASB. The new converged expected loss model focuses on the absolute level and subsequent changes of credit quality of financial assets and reflects the general pattern of deterioration in credit quality through so called 'three-bucket' approach. The IASB intends to issue the new proposals for public comment in 2012.

EFRAG did not take any decisions at this meeting.

IASB Project *Revenue Recognition*

EFRAG discussed its preliminary views on the tentative decisions reached by the IASB in relation to the revenue recognition project focusing on the criteria for applying percentage-of-completion accounting and

options to extend and cancel a contract. The revised proposals on the project are expected to be published for comments in November 2011.

In relation to the criteria for applying percentage-of-completion accounting, EFRAG noted that during the re-deliberations process the IASB had addressed a number of issues raised in EFRAG's comment letter in response to the 2010 Exposure Draft. EFRAG has tentatively decided to acknowledge that fact in its draft comment letter on the revised proposals.

EFRAG will continue discussing its preliminary position on the revised proposals at the next meeting.

During the session held together with the European national standard setters, EFRAG and CFSS members were updated on the arrangements for the European field-testing of the forthcoming revised proposals on revenue recognition, which is conducted in cooperation with the European national standard setters and in close coordination with the IASB. The objective of the field-testing is to identify potential implementation and application difficulties; assess the directions of any changes in elements of entities' financial position and performance; and estimate the effort required to implement and apply the proposals. EFRAG made a public call for participants in the field-testing on its website and was assisted in identifying participants by the European National Standard Setters. Forty three companies across Europe representing telecommunications, software and technology, pharmaceutical and healthcare, utilities and services industries, and industries operating under long-term contracts (e.g., construction and engineering) have been selected to participate in the field-testing. The tests will be carried out once the Exposure Draft is issued by the IASB. The findings made during the field-testing will be reported to the IASB and will be considered by EFRAG in finalising its comment letter in response to the forthcoming proposals.

IASB Draft Q&As on IFRS for SMEs

On 4 October 2011, EFRAG finalised its draft comment letter to the IASB in response to the third batch of the draft Q&As on IFRS for SMEs.

Similar to the concern expressed in EFRAG's comment letter in response to the second batch of the draft Q&As, EFRAG noted that Q&As did not focus on a limited number of pervasive issues, as they should according to the terms of reference and operating procedures for the SME Implementation Group.

EFRAG recommended not issuing any of the Q&As. The draft comment letter is available on EFRAG's website. The comment deadline is 18 November 2011.

During its monthly meeting, EFRAG discussed its preliminary position on the forthcoming new batch of draft Q&As on IFRS for SMEs, which is expected to be issued for comments in the near future.

IASB Agenda Consultation

In August 2011, EFRAG issued its draft comment letter in response to the IASB Agenda Consultation. EFRAG also decided to stimulate the debate in Europe and to seek views of European constituents on the subject by organising outreach meetings in partnership with the European national standard setters. Meetings will be held in Frankfurt, Copenhagen, Oslo, Amsterdam, Stockholm, Warsaw and Brussels. CFSS members received an update on the outreach initiative.

The draft comment letter and the details of the outreach meetings are available on EFRAG's website. The comment deadline for the draft comment letter is 15 November 2011.

EFRAG Proactive Project *Income Taxes*

CFSS members received an update on the content and the status of the Discussion Paper being developed by EFRAG together with the national standard setters of the UK (ASB) and Germany (GASB) on the accounting for corporate income tax. Before publication, the Discussion Paper will be forwarded to the European national standard setters, so they can indicate within 30 days whether their organisation wants to be associated with it. The Discussion Paper will be published shortly after that.

EFRAG Proactive Project *Disclosure Framework for the Notes to the Financial Statements*

EFRAG received an update on the status of the project, in particular, on the revised project plan and the cooperation with the US FASB project team. Additionally, it was updated on the components of the *Disclosure Framework for the Notes to the Financial Statements* and how the framework would assist in the development and application of disclosures.

EFRAG noted that disclosure requirements should be based on the information needs of the users of financial statements and that the project should describe how disclosures should provide relevant information about risk exposure of entities. It also noted that the proposals, which will be included in the forthcoming Discussion Paper, should be tested to illustrate their impact on the existing requirements.

The Discussion Paper on the project is expected to be published in the first quarter of 2012.

EFRAG Proactive Project *Considering the Effects of Accounting Standards*

EFRAG received an update on the comments received in response to the Discussion Paper *Considering the Effects of Accounting Standards* (the DP), which was published in January 2011 together with the national standard setter of the UK (ASB). The DP suggested that further integration of effects analysis in the standard-setting due process would be an important step in strengthening that process. The DP also included proposals in respect of the effects to be considered, the parties to be responsible for the performance of effects analysis, and the organisation of the process.

The respondents to the DP generally agreed that the consideration of effects of accounting standards should be further embedded into the standard-setting due process. They believed that it would make the process more efficient, effective and evidence-based, and that it would improve the communication with stakeholders by clearly informing them about the objective of a project and the expected effects. The respondents, however, had diverging views on individual aspects of the process proposed in the DP.

EFRAG will issue a feedback statement reflecting the comments received on the DP in the due course.

Developments affecting the implementation of IFRS in the United States

EFRAG and CFSS members received an update on the developments affecting the implementation of IFRS in the United States.