

December 2012

Summary of EFRAG Technical Expert Group and Consultative Forum of Standard Setters meeting December 2012

EFRAG TEG held a conference call on 29 November 2012 to approve EFRAG's response to the IASB's *Request for Information* in the Post-implementation Review of IFRS 8 *Operating Segments*.

From 11 to 14 December 2012, EFRAG TEG held its monthly meeting. The first two days were held together with European National Standard Setters in EFRAG's Consultative Forum of Standard Setters. The following topics were discussed:

- Preparation for EFRAG-IASB public meeting
- IAS 19 *Employee Benefits*
- IASB Exposure Draft *Classification and Measurement: Limited Amendments to IFRS 9* and IASB project *IFRS 11 – Acquisition of an Interest in a Joint Venture*
- EFRAG proactive project *Capital providers' Use of Financial Statements*
- IASB project *Conceptual Framework*
- Agenda for future EFRAG CFSS meetings
- IASB Exposure Draft *Annual Improvements to IFRSs 2011-2013 Cycle*
- IASB Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation*
- IASB Exposure Draft *Share of Other Net Asset Changes*
- IFRS 9 *Financial Instruments* Phase III – Hedge Accounting
- IASB Project *Leases*
- *Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)*
- IASB Exposure Draft *Classification and Measurement: Limited Amendments to IFRS 9*
- EFRAG proactive project *The Role of the Business Model in Financial Reporting*
- EFRAG TEG discussed a working draft of the first five chapters of a discussion paper. EFRAG TEG directed the EFRAG staff on how to improve the content of the discussion.
- IASB Request for Information *Comprehensive Review of the IFRS for SMEs*
- IFRS Interpretations Committee agenda decision *Income and expenses arising on financial instruments with a negative interest rate*

Highlights

Draft Endorsement Advices

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)

EFRAG TEG discussed and approved a draft Endorsement Advice. EFRAG tentatively supports the adoption of the amendments and recommends their endorsement.

Comments are invited on the draft Endorsement Advice and effects study report by 21 January 2013.

Comment letters

EFRAG Update is published for the convenience of EFRAG's constituents. All conclusions reported are tentative and may be changed or modified at future meetings.

IASB Post-implementation Review of IFRS 8 Operating Segments

EFRAG TEG approved EFRAG's final response to the IASB's *Request for Information*. The response summarised evidence received from constituents across Europe, including at EFRAG's autumn 2012 series of outreach events.

IASB Exposure Draft Annual Improvements to IFRSs 2011-2013 Cycle

EFRAG TEG approved EFRAG's draft comment letter in response to the Exposure Draft. In its draft comment letter, EFRAG supported most of the proposals, but raised concerns regarding what appeared to be unnecessary amendments and amendments to the bases of conclusions of standards.

Comments are invited on the draft comment letter by 1 February 2013.

IASB Exposure Draft Clarification of Acceptable Methods of Depreciation and Amortisation

EFRAG TEG approved EFRAG's draft comment letter in response to the Exposure Draft. In its draft comment letter, EFRAG supported the IASB's efforts to clarify current requirements, but identified an apparent contradiction between the amendment and the accompanying Basis for Conclusions.

Comments are invited on the draft comment letter by 11 March 2013.

Post-implementation Review of IFRS 8 Operating Segments

EFRAG TEG approved EFRAG's formal response to the IASB's *Request for Information*. This reflected evidence gathered from European constituents during EFRAG's outreach activities, conducted in partnership with European National Standard Setters and user organisations and with the involvement of the IASB; responses to questionnaires and EFRAG staff reviews of operating segment disclosures in financial statements.

The evidence suggests that no fundamental overhaul of IFRS 8 is needed, however that the implementation of IFRS 8's underlying management approach can be improved, based on comments received (including from users, preparers, auditors and regulators) in the level of aggregation of operating segments, the identification of the Chief Operating Decision Maker, reconciliations of line items between the total for reportable segments and the values reported in the primary statements, and the preparation of entity-wide information. The evidence gathered corroborated the findings of ESMA's 2011 report and EFRAG advised the IASB to discuss the application of the standard in practice in detail with regulators, including ESMA, and auditors before any further standard-setting effort is undertaken.

Preparation for EFRAG-IASB public meeting

EFRAG staff presented to the EFRAG CFSS and EFRAG TEG members the proposed points for discussion with the IASB in the next EFRAG-IASB public meeting scheduled for 18 December 2012.

The members were supportive to most of EFRAG's proposed messages. There were concerns regarding the uncertainty of the moving timelines for the completion of both IFRS 9 *Financial Instruments* and IFRS 4 *Insurance Contracts*. Some members however thought that it was too early for EFRAG to be discussing messages with the IASB regarding IFRS 4.

There were concerns on the IASB agenda. EFRAG informed the members that the IASB's agenda was generally consistent with constituents' input received calling for a period of calm, further work on the conceptual framework and to address the issue of improving the quality of existing disclosures. The members proposed adding to the discussion the limited scope

amendments to clarify some aspects of IAS 27 *Separate Financial Statements* and IFRS 11 *Joint Operations*.

The views provided by the NSS at the joint meeting will assist EFRAG in the public meeting with the IASB.

IAS 19 Employee Benefits

EFRAG TEG and CFSS members received an update on the discussions of the IFRS Interpretations Committee on various application issues of IAS 19 (2011) *Employee Benefits*. The discussion was focused on how entities should determine the discount rate used to discount defined benefit obligations considering the impact in certain European jurisdictions of the current sovereign debt crisis and economic downturn, and the fact that deep markets for corporate bonds might no longer exist in certain jurisdictions. EFRAG CFSS members explained how their jurisdictions were affected by the issue and expressed their concerns about the significant impact that the discount rate has on the amounts recognised in the financial statements.

EFRAG TEG and CFSS members decided to include this topic onto the agenda for the next EFRAG-IASB meeting on 18 December 2012.

IASB Exposure Draft *Classification and Measurement: Limited Amendments to IFRS 9* and IASB project *IFRS 11 - Acquisition of an Interest in a Joint Venture*

EFRAG TEG and CFSS members received an update on the early input received from National Standard Setters regarding the Exposure Draft and proposed amendments. EFRAG aims to obtain early input from National Standard Setters before the IASB issues proposals on particular topics so that they have the opportunity to influence EFRAG's preliminary views, as discussed in the EFRAG CFSS October 2012 meeting.

The preliminary views provided by National Standard Setters will help EFRAG TEG in its discussions resulting in EFRAG's draft comment letter.

EFRAG proactive project *Capital providers' Use of Financial Statements*

In June 2011, EFRAG PRC launched a new pro-active project on understanding how capital providers use financial statements. The aim of the project was to shed light on how various types of European capital providers use financial information for decision making, and how they manipulate and analyse this information.

EFRAG decided that the first step in the project should be a review of the existing literature dealing with the issue. EFRAG agreed with the Institute of Chartered Accountants of Scotland to co-sponsor such a review.

EFRAG CFSS members received the preliminary results of the review. The results showed that financial statement information was important for many different types of users, but the use (and the needs) of these users were different. The results, for example, indicated that the use could be different for decisions related to forecasts and decisions related to assessing past performance of an entity or an entity's management. In addition, the results showed that within the EU there were big differences in how entities were financed, and hence how important the different groups of users were, and reflected that there was room for more research in the area.

EFRAG expects to receive the complete literature review by the end of December 2012. It will decide on further actions in 2013.

IASB project *Conceptual Framework*

The IASB is expected to issue a discussion paper on the last chapters of the Conceptual Framework in July 2013. To prepare itself and its constituents for their comments in response to this discussion paper, EFRAG will, among other things, issue short discussion papers (called bulletins) in co-operation with National Standard Setters.

EFRAG CFSS members received a presentation on the IASB's plans in relation to finalising the Conceptual Framework. Four draft bulletins were presented in the meeting. The timing and types of activities to be performed by EFRAG and National Standard Setters were considered. It was also discussed how to decide on the topics for which bulletins should be issued.

Agenda for future EFRAG CFSS meetings

EFRAG CFSS members discussed the practical aspects of the agenda setting process of future EFRAG CFSS meetings so as to involve the European National Standard Setters more actively. EFRAG CFSS members agreed to informally identify the topics they believe are of a high priority in advance of each meeting, in order to ensure that those with a wide interest are included.

IASB Exposure Draft *Annual Improvements to IFRSs 2011-2013 Cycle*

EFRAG TEG discussed and finalised EFRAG's draft comment letter in response to the Exposure Draft *Annual Improvements to IFRSs 2011-2013 Cycle* issued by the IASB on 20 November 2012.

In its draft comment letter, EFRAG agreed with most proposals in the ED and with the objective the IASB is trying to achieve, but it believed that the proposed amendment to IFRS 1 did not merit immediate attention through the annual improvement process as it was unnecessary.

In addition, EFRAG believed that the IASB should not make amendments to the bases for conclusions of standards, unless it wished to correct outright errors.

In EFRAG's view, amendments to bases for conclusions could not take the place of actual standard setting. Furthermore, EFRAG noted that such amendments did not form part of the standards themselves and hence do not affect IFRSs as endorsed in the European Union.

Comments are invited on the letter by 1 February 2013.

IASB Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation*

In its December 2012 meeting, EFRAG TEG discussed and approved its draft comment letter on the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed Amendments to IAS 16 and IAS 38)* that was issued by IASB on 30 November 2012.

In its letter, EFRAG supported the IASB's efforts to clarify the current requirements regarding the use of revenue-based methods of depreciation and amortisation.

However, EFRAG believed that the IASB should remove the seeming contradiction between the standard and the Basis for Conclusions by incorporating into the body of the standard the reasoning that there are circumstances where revenue might be an appropriate proxy for the use of an asset.

Comments are invited on the letter by 11 March 2013.

IASB Exposure Draft *Share of Other Net Asset Changes*

At its December 2012 meeting, EFRAG TEG discussed an initial draft comment letter on the Exposure Draft issued by the IASB on 22 November 2012. The IASB proposes that an investor should recognise in its own equity its share of the investee's other net asset changes.

EFRAG TEG members had differing views on this topic. Some members agreed with the IASB's proposal, while other members believed that recognising such changes in the investor's equity would be inconsistent with some of the concepts and principles in existing IFRS literature, including the requirement in IAS 1 to present within the statement of changes in equity only transactions with owners. However, these EFRAG TEG members had mixed views about how to account for an investor's share of the investee's other net asset changes.

- (a) While some believed that changes in net assets at the level of the investee should be reflected in the investor's accounts, they did not agree that these changes should be reflected in equity.
- (b) Other EFRAG TEG members believed that 'equity' changes in an investee accounted for under the equity method, should not be reflected in the investor's accounts since, in their view, the investor is not a party to the 'equity' transaction.

A revised draft comment letter will be discussed in an EFRAG TEG conference call on 20 December 2012.

IFRS 9 *Financial Instruments Phase III - Hedge Accounting*

EFRAG TEG members discussed a draft of an EFRAG letter to the IASB on its Review Draft IFRS 9 *Financial Instruments: Phase III Hedge Accounting* based on the results from EFRAG's field-testing exercise. EFRAG TEG members noted the important improvements introduced by the Review Draft in the hedge accounting requirements including:

- (a) the hedge effectiveness testing requirements;
- (b) the treatment of the time value of options and the treatment of forward points;
- (c) the possibility to designate aggregated exposures as eligible hedged item;
- (d) the ability to designate risk components as eligible hedged item; and
- (e) the ability to rebalance hedge relationships.

During the meeting it was noted that there are still a number of complexities associated with the model due to the large number of exceptions, restrictions and options as well as drafting issues. The Review Draft requires considerable effort to understand even from those who are financial instruments specialists, and contains many cross references, making it difficult to read as a standalone document. Additional examples clarifying the standard for non-financial companies would be welcome.

A revised letter will be discussed at an EFRAG TEG conference call on Thursday 20 December.

IASB Project *Leases*

EFRAG TEG discussed recent developments around the Leases project and received an update on the FRC's current position, expressing support to the IASB project on replacing IAS 17, but with a number of concerns on the current proposals. EFRAG TEG members welcomed this development. It remained to be seen how the new ED would reflect the IASB's recent decision that the balance sheet presentation should only be for those leases that contain a financing element.

EFRAG TEG held a series of discussions on measurement issues to establish preliminary views to be set out in the EFRAG draft comment letter. In particular, some EFRAG TEG members

thought that options did not meet the definition of liabilities, and should be recognised only when the entity had no realistic alternative to avoid the extension, while others supported the IASB's current proposals. EFRAG TEG did not support the use of different impairment requirements being applied to right-of-use assets under the Single Lease Expense approach, but instead supported the use of IAS 36 *Impairment of Assets*. Lease back, presentation and disclosure requirements will be discussed in January.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)

EFRAG TEG discussed and approved a draft Endorsement Advice, setting out EFRAG's initial assessment that the amendments satisfy the technical criteria for EU endorsement, and EFRAG should therefore recommend their endorsement.

Comments are invited on the draft endorsement advice by 21 January 2013.

IASB Exposure Draft Classification and Measurement: Limited Amendments to IFRS 9

EFRAG TEG discussed a draft comment letter on the Exposure Draft issued by the IASB on 28 November 2012 to clarify and propose specific changes to the measurement and classification requirements for financial assets in IFRS 9.

EFRAG TEG appreciated that the IASB had considered its request to address accounting mismatches arising from the interaction between the classification and measurement requirements in IFRS 9 and the future IFRS on insurance contracts. However, EFRAG TEG members held divergent views on the appropriateness of introducing a third business model in IFRS 9. EFRAG TEG welcomed the fact that the IASB had included an effect analysis in the basis for conclusions at the exposure draft stage.

A revised draft comment letter will be discussed in an EFRAG TEG conference call on 20 December 2012.

EFRAG proactive project The Role of the Business Model in Financial Reporting

EFRAG TEG discussed a working draft of the first five chapters of a discussion paper. EFRAG TEG directed the EFRAG staff on how to improve the content of the discussion.

IASB Request for Information Comprehensive Review of the IFRS for SMEs

EFRAG TEG finalised EFRAG's final comment letter in response to the *Request for Information* ('the RFI'). In this final comment letter, EFRAG notes that many constituents found the purpose of the IFRS for SMEs and the objective of the RFI unclear, making it difficult to respond to the RFI.

Some respondents to EFRAG's draft comment letter thought that non-listed subsidiaries of listed parent entities should be considered an important group of users of the IFRS for SMEs. These entities wanted to be able to prepare financial statements in accordance with the recognition and measurement requirements used for the consolidation under full IFRS, but with fewer disclosures. EFRAG believed that it would be relevant for the IASB to consider whether a regime for these entities should be developed, as it had been in some jurisdictions. However, EFRAG believed that if the IASB decided to develop such a regime it should not be introduced through the IFRS for SMEs, but by other means.

Some of the questions included in the RFI asked whether changes to full IFRS should be incorporated into the IFRS for SMEs. EFRAG generally thought that the changes should only be incorporated if they represented a solution to an identified and documented problem for SMEs and/or had proven useful for entities applying full IFRS.

As expressed in its comment letter on the exposure draft on the IFRS for SMEs, EFRAG was generally against including options in the IFRS for SMEs, as it, among other things, would reduce comparability. In some cases, however, EFRAG could see benefits of including options to facilitate the adoption of the IFRS for SMEs. If the introduction of these options would result in more entities being able to prepare financial statements in accordance with the IFRS for SMEs, it would enhance overall comparability.

EFRAG expects to issue its final comment letter and feedback statement by the end of 2012.

IFRS Interpretations Committee agenda decision *Income and expenses arising on financial instruments with a negative interest rate*

Following comments from constituents and a letter from the German ASCG to the IFRS Interpretations Committee, EFRAG TEG discussed whether EFRAG should also write a letter to the Committee about the rejection notice on income and expenses arising on financial instruments with a negative interest rate. A decision will be taken at an EFRAG TEG conference call on 20 December 2012