

## Summary of EFRAG meetings held in September - October 2010

On 20 September 2010, EFRAG held a meeting by public conference call to discuss:

- IFRS Interpretations Committee Draft IFRIC Interpretation, *Stripping Cost in the Production Phase of a Surface Mine*
- IFRS Interpretations Committee draft rejection notice on *Put options written over non-controlling interests*
- IASB Exposure Draft, *Removal of Fixed Dates for First-time Adopters – Proposed amendments to IFRS 1*
- IASB Exposure Draft, *Leases*

On 22 September 2010, EFRAG held an additional one-day meeting and discussed:

- IASB project, *Hedge Accounting*
- IASB project, *Asset and Liability Offsetting*
- FASB Exposure Draft, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities*
- IASB Exposure Draft, *Presentation of Items of Other Comprehensive Income*
- IASB Exposure Draft, *Deferred Tax: Recovery of Underlying Assets – Amendments to IAS 12 Income Taxes*

On 5 October 2010, EFRAG met with the European National Standard Setters in EFRAG's Consultative Forum of Standard Setters (CFSS) to discuss:

- IFRS Interpretations Committee draft rejection notices
- IASB Exposure Draft, *Leases*
- EFRAG Outreach Activities on *Financial Statement Presentation*
- XBRL

On 6 and 7 October 2010, EFRAG held its monthly meeting and discussed:

- IASB Exposure Draft, *Deferred Tax: Recovery of Underlying Assets – Amendments to IAS 12 Income Taxes*
- IASB Exposure Draft, *Revenue Recognition: Revenue from Contracts with Customers*
- IASB project, *Hedge Accounting*
- IFRS Interpretations Committee draft rejection notice on *Put options written over non-controlling interests*
- IFRS Interpretations Committee draft rejection notices on other issues
- EFRAG proactive project, *Disclosure Framework*
- EFRAG proactive project, *Business Model*
- EFRAG joint project with FEE, *Bifurcation*
- EFRAG consultation on proactive work

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

## Highlights

### **Comment letters to the IASB**

EFRAG finalised its comment letter to the IASB on the Exposure Draft, *Presentation of Items of Other Comprehensive Income*. EFRAG objects to the IASB's initiative to proceed with the proposal to present all non-owner changes in equity in a single statement of comprehensive income, because it would not result in any change or improvement to current financial reporting.

EFRAG finalised its comment letter to the IFRS Interpretations Committee on the tentative agenda decision on the accounting on put options written over non-controlling interests ('NCI puts'). EFRAG believes that it is inappropriate to include interpretations – with potentially widespread consequences – in the wordings for rejection on complex, long-running issues. However, we agree with the Interpretations Committee's decision not to take this item onto its agenda.

In September and October 2010, EFRAG invited comments on the following draft comment letters:

- IFRS Interpretations Committee, Draft IFRIC Interpretation, *Stripping Cost in the Production Phase of a Surface Mine*. EFRAG supports the Interpretations Committee in their efforts to resolve diversity in practice. However, we do not believe that the Draft Interpretation will appropriately achieve this.
- IASB Exposure Draft, *Removal of Fixed Dates for First-time Adopters – Proposed amendments to IFRS 1*. The draft comment letter is supportive of the proposals.
- IASB Exposure Draft, *Leases*. EFRAG supports the decision to develop an accounting model to replace the existing IAS 17, provided that the proposals offer an effective improvement over the existing requirements. Although EFRAG acknowledges the conceptual merits of some of the proposals included in the ED, we are not persuaded that the ED offers an effective improvement.
- IASB Exposure Draft, *Deferred Tax: Recovery of Underlying Assets – Amendments to IAS 12 Income Taxes*. EFRAG disagrees with the use of an exception to the measurement principles in IAS 12 to resolve the issues being addressed in the ED. In EFRAG's view, the issue should be addressed by extending application guidance on the measurement principle.
- IFRS Interpretations Committee draft rejection notices on *IAS 36 Impairment of Assets – Calculation of value in use*. EFRAG agreed to write to the Interpretations Committee requesting that the words, 'rarely be appropriate,' be removed from the rejection notice and to recommend that the rejection notice clarify that a dividend discount model can be used by entities in the consolidated accounts, provided that the requirements set out in paragraphs 30-57 of IAS 36 are met.

### **Comment letters to the FASB**

EFRAG finalised its comment letter to the FASB on the Exposure Draft, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities*. In EFRAG's view, the FASB proposals do not provide a basis for a high-quality standard on accounting for financial instruments. The comment letter is supportive of the broad direction set by the IASB in its project to replace IAS 39, *Financial Instruments: Recognition and Measurement* as the basis for the development of a converged standard.

## IASB Exposure Draft *Leases*

During its meeting held by public conference call on 20 September 2010, EFRAG finalised its draft comment letter in response to the IASB Exposure Draft, *Leases* ('the ED'). EFRAG supports the decision to develop an accounting model to replace the existing IAS 17 standard, provided that the proposals offer an effective improvement over the existing requirements. Although EFRAG acknowledges the conceptual merits of some of the proposals included in the ED, it is not persuaded that the ED offers an effective improvement. The main aspects addressed in EFRAG's draft comment letter are:

- *Scope* – EFRAG disagrees with the exclusion of intangible asset leases from the scope of the ED;

→

→

- *Lessee accounting* – EFRAG supports the right-of-use model for lessees, provided a clear and operational distinction between leases and service agreements is developed;
- *Lessor accounting* – EFRAG is concerned about the complexity of the ‘hybrid’ accounting model for lessors, which is based on the derecognition model and the performance obligation model, and confirmed its preference for a single, partial derecognition model;
- *Renewal options and contingent rents* – EFRAG believes that amounts due under options and contingent rentals should not be included in the measurement of the lease assets and liabilities;
- *Sale and leaseback transactions* – EFRAG disagrees with the proposals in the ED in respect of the sale and leaseback transactions, since it contradicts the premise that an asset is a bundle of rights. EFRAG believes that, in such a contract, the lessee sells all the rights attached to the asset, except for the right-of-use that is retained in the lease.

The draft comment letter is available on EFRAG’s website. The comment deadline is 26 November 2010.

At the October CFSS meeting, members received an update on the main messages included in EFRAG’s draft comment letter on leases. CFSS members provided preliminary feedback on the draft comment letter and discussed the scope of the Exposure Draft, the definition of a lease, lessor accounting, and the accounting treatment of options and contingent rentals.

## **IASB Exposure Draft *Revenue from Contracts with Customers***

---

At its October meeting, EFRAG discussed the comment letters received in response to EFRAG’s draft comment letter to the IASB on the Exposure Draft *Revenue Recognition: Revenue from Contracts with Customers*. Based on the comments received, it was tentatively decided to amend EFRAG’s comment letter to:

- include a general comment that the costs of applying the requirements in the Exposure Draft seemed high for preparers and that the IASB should examine whether the benefits would exceed these costs in all circumstances;
- recommend that the transaction price should be allocated to separate performance obligations within a contract based on the actual margins of each performance obligation, rather than the standalone selling price of each performance obligation;
- recommend that an entity should distinguish between statutory and extended warranties. For statutory warranties the expected costs to fulfil the warranty should be provided for. An extended warranty should be accounted for as a separate performance obligation. Part of the transaction price should therefore be allocated to this separate performance obligation;
- amend the description of the alternative model proposed by EFRAG for revenue recognition. Among other things, the model proposed by EFRAG should not be described as an ‘activity-based,’ model as this had led people to misunderstand the alternative model.

EFRAG agreed to approve its final comment letter in response to the Exposure Draft at a conference call on 19 October 2010.

## **IFRS Interpretations Committee Draft Rejection Notice on *Put Options Written over Non-controlling Interests***

---

EFRAG finalised its comment letter to the Interpretations Committee on the tentative agenda decision on the accounting on put options written over non-controlling interests (‘NCI puts’).

In its comment letter, EFRAG agrees with the Interpretations Committee that the subsequent measurement of NCI puts is a matter that warrants action from the IASB, because there is significant divergence in practice. EFRAG believes that it is inappropriate to include interpretations – with

→

→

potentially widespread consequences – in the wordings for rejection on complex, long-running issues. As the wording for rejection does not address the issue raised with the Interpretations Committee in May 2010 in a balanced manner (i.e. the perceived conflict between IAS 27 and IAS 32/39), we believe that the IFRS Interpretations Committee should redraft its tentative wording for rejection so that it no longer refers to IAS 32/39. However, we agree with the Interpretations Committee's decision not to take this item onto its agenda.

## **IFRS Interpretations Committee Draft Rejection Notice on IAS 32 and IAS 36**

---

EFRAG has received two submissions from constituents expressing concern about the wording of the IFRS Interpretations Committee's tentative rejection notices:

- The first submission relates to uncertainty in the application of IAS 12, *Income Taxes* regarding the recognition of deferred tax assets for unrealised losses on available-for-sale debt securities. The drafting of the tentative decision states that an entity's decision to hold an available-for-sale debt security until maturity does not meet the definition in paragraph 30 of IAS 12 of a tax planning opportunity. In addition, the tentative decision observes that the guidance in IAS 12 requires an entity to assess the probability of realising deferred tax assets on a combined basis, rather than on a separate basis. The Interpretations Committee asked the project staff to carry out further work on the issue, before it finalised its decision at its meeting in November 2010.

EFRAG agreed to consider its further actions following the final decision on the issue by the Interpretations Committee at its November 2010 meeting.

- The second issue relates to whether an entity can use a dividend discount model under IAS 36, *Impairment of Assets* when calculating value in the use of a subsidiary, that is considered to be a cash-generating unit in the consolidated accounts of a parent entity. The drafting of the tentative decision states that the use of a dividend discount model would rarely be appropriate when calculating value in use of a cash-generating unit in the consolidated financial statements.

EFRAG discussed the Interpretations Committee's decision not to take this item onto its agenda and the wording of the rejection notice. EFRAG agreed that the wording of the rejection was not appropriate and that it would write to the Interpretations Committee and ask that the words 'rarely be appropriate' be removed from the rejection notice and recommend that the rejection notice clarify that a dividend discount model can be used by entities in the consolidated accounts provided that the requirements set out in paragraphs 30-57 of IAS 36 are met. The draft comment letter is available on EFRAG's website. The comment deadline is 27 October 2010.

## **IFRS Interpretations Committee Draft Rejection Notices (CFSS)**

---

At the October CFSS meeting, members received an update on EFRAG's approach towards the IFRS Interpretations Committee's rejection notices and asked members for recommendations on how to deal with these. In recent months, some constituents expressed concern that wordings for rejection were written, in some cases, as if they were interpretations of existing IFRS material, rather than rejection decisions.

CFSS members encouraged EFRAG to respond when there was a significant issue with wording of the published rejection notices. It was suggested that EFRAG should write to the Trustees of the IFRS Foundation to express its concerns.

## **IASB Project Hedge Accounting**

---

In view of the replacement of IAS 39 by IFRS 9, *Financial Instruments*, the IASB is currently considering changes to the requirements for hedge accounting. The aim of this third phase of IFRS 9 is to increase the decision-usefulness of financial statements by reflecting an entity's risk management strategy in its

→

→

financial reporting. The Exposure Draft is expected to be published in the fourth quarter of 2010. The tentative decisions to date have focused on the development of a hedging model for closed portfolios.

At its October meeting, EFRAG held an initial discussion on the hedge accounting project and considered the IASB's main tentative decisions on hedge accounting for closed portfolios. No decisions were taken. EFRAG will discuss hedge accounting again at its November 2010 meeting.

## **IASB Project *Asset and Liability Offsetting***

---

EFRAG members received an update on the objective and status of the IASB project, *Asset Liability Offsetting*, which focused on the developments of IFRS and US GAAP in this area. EFRAG held a preliminary discussion on the relevance of this issue for the comparability of US GAAP and IFRS statements of the financial position of financial institutions and on the significance of legal enforceability of a Master Netting Agreement. No decisions were taken.

## **EFRAG Joint Project with FEE *Bifurcation***

---

EFRAG and FEE have jointly undertaken a project to explore whether a proposal could be developed to address concerns raised by European constituents about the elimination of bifurcation of embedded derivatives on the asset side.

EFRAG members received an update on whether and how later phases in the development of IFRS 9, *Financial Instruments*, might influence the boundary between amortised cost and fair value. In particular, EFRAG members considered whether a principles-based approach to bifurcation of embedded derivatives could be developed to replace the existing requirements in IAS 39, *Financial Instruments: Recognition and Measurement*. No decisions were made. EFRAG will continue working on this issue.

## **FASB Exposure Draft *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities***

---

During its meeting on 22 September 2010, EFRAG finalised its comment letter in response to the FASB Exposure Draft, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities* ('the ED').

In EFRAG's view, the FASB proposals do not provide a basis for a high-quality standard on accounting for financial instruments. EFRAG's comment letter supports the broad direction set by the IASB in its project to replace IAS 39, *Financial Instruments: Recognition and Measurement*, as the basis for the development of a converged standard. More specifically, EFRAG supports the following elements in the IASB's approach:

- classification criteria based on the characteristics of the financial instruments and the business model used by the entity in managing those financial instruments;
- a mixed measurement model that allows financial instruments to be reported at either amortised cost or fair value, depending on the business model;
- reclassification required when there is a change in the conditions that lead to initial classification;
- primary financial statements that reflect only one measurement attribute for each financial instrument;
- impairment of financial assets measured at amortised cost based on an expected loss approach that uses all available credit-related information, including forecasts of future events and future economic conditions; and

→



→

- recognition of fair value changes due to changes in an entity's own credit risk outside profit or loss, when liabilities are designated under the fair value option, except in extremely rare circumstances where the fair value changes of financial assets are directly linked to an issuer's own credit risk.

EFRAG considers that both Boards should work together to develop a standard, starting from the principles in IFRS 9, *Financial Instruments* and incorporating several improvements that are listed in the comment letter. We note that European constituents express strong support for the adoption of a mixed measurement model for financial instruments, as opposed to the fair value model proposed by the FASB.

## IASB Exposure Draft *Presentation of Items of Other Comprehensive Income*

---

EFRAG finalised its comment letter in response to the IASB's Exposure Draft, *Presentation of Items of Other Comprehensive Income (Proposed amendments to IAS 1)*.

In its comment letter, EFRAG objects to the IASB's initiative to proceed with the proposal to present all non-owner changes in equity in a single statement of comprehensive income. EFRAG believes that before discussing a single statement of comprehensive income, a proper debate is necessary on fundamental issues related to performance reporting, such as:

- the notion of performance and its relationship with business models;
- the content of performance statement(s), including the principles that underpin comprehensive income; and
- recycling.

EFRAG does not support the proposal because it would not result in any change or improvement to the current financial reporting.

EFRAG is supportive overall of the proposal to present separately items of other comprehensive income that are reclassified to profit or loss (recyclable) and those that are not reclassified to profit or loss (non-recyclable); and to allocate income tax to separate groups of other comprehensive income. However, EFRAG believes that it would be more efficient to finalise the disaggregation amendments as part of the Annual Improvements process, without a separate re-exposure within the next Annual Improvements cycle.

The comment letter is available on the EFRAG website.

## EFRAG Outreach Activities on *Financial Statement Presentation (CFSS)*

---

At the October CFSS meeting, members considered an update on the progress made by EFRAG and the National Standard Setters in organising an outreach event on financial statement presentation, in cooperation with the IASB.

### XBRL (CFSS)

---

CFSS members also attended an educational session on the eXtensible Business Reporting Language (XBRL) that was presented by Gilles Maguet of XBRL Europe and Olivier Servais of the IFRS Foundation. CFSS members shared their experiences with XBRL in their own jurisdictions.

## **IASB Exposure Draft *Deferred Tax: Recovery of Underlying Assets - Amendments to IAS 12 Income Taxes***

---

EFRAG finalised its draft comment letter in response to the IASB's Exposure Draft, *Deferred Tax: Recovery of Underlying Assets – Proposed amendments to IAS 12* ('the ED'). The ED introduces an exception to the measurement principles in IAS 12. Depending on the facts and circumstances, under the current IAS 12 model, an entity would base the measurement of deferred tax on the tax consequences of recovering the carrying amount of the underlying asset, as follows:

- entirely by sale;
- entirely through use; or
- partially by sale and partially by use.

The ED proposes to amend this aspect of IAS 12 and aims to provide a practical approach in those cases where it is difficult or subjective to determine the manner in which an entity expects to recover the carrying amount of its assets.

EFRAG agrees that the existing IAS 12 lacks guidance on the accounting for income tax in relation to assets for which the tax consequences depend on the way their carrying amount is recovered. For that reason, EFRAG supports the IASB's efforts to address the issue. However, EFRAG disagrees with the use of an exception to the measurement principles in IAS 12 to resolve the issues being addressed in the ED. In EFRAG's view, the issue should be addressed by extending application guidance on the measurement principle. This would be clearer and would produce the right answer based on the 'manner of recovery' of the underlying asset.

The draft comment letter is available on EFRAG's website. The comment deadline is 6 November 2010.

## **IASB Exposure Draft *Removal of Fixed Dates for First-time Adopters - Proposed amendments to IFRS 1***

---

During its meeting held by public conference call on 20 September, EFRAG discussed the IASB Exposure Draft *Removal of Fixed Dates for First-time Adopters Proposed amendments to IFRS 1*.

Many entities, particularly in jurisdictions that will be adopting IFRSs, will need to apply IFRS 1 in the near future. The fixed dates in IFRS 1 result in exceptions and exemptions that are largely irrelevant for those entities, as they only apply to transactions that occurred before 2004.

The draft comment letter is supportive of the proposals. The draft comment letter is available on EFRAG's website. The comment deadline is 21 October 2010.

## **IFRS Interpretations Committee Draft IFRIC Interpretation *Stripping Cost in the Production Phase of a Surface Mine***

---

During its meeting held by public conference call on 20 September 2010, EFRAG finalised its draft comment letter in response to the IFRS Interpretations Committee's Draft IFRIC Interpretation, *Stripping Cost in the Production Phase of a Surface Mine*. EFRAG supports the Interpretations Committee in its efforts to resolve diversity in practice. However, EFRAG does not believe that this Draft Interpretation appropriately achieves this.

EFRAG believes that the Committee should consider requiring application of the accounting model in IAS 16 to all forms of stripping costs. EFRAG thinks that this would avoid introducing unnecessary complexity in IFRSs. The draft comment letter is available on EFRAG's website. The comment deadline is 19 November 2010.

## **EFRAG Proactive Project *Disclosure Framework***

---

At its October meeting, EFRAG members received an update on the status of the project and were asked for their input on the current thinking. The following key messages were expressed during the discussion:

- the project should consider the work on the Conceptual Framework and Financial Statement Presentation projects;
- the project should consider the implication of electronic reporting by preparers;
- it would be useful to develop some type of guidance for the preparation of a summary of the financial statements where key figures and messages should be presented to the readers;
- the project should properly consider the cost of providing information;
- extensive literature on disclosures already exists. Therefore, care should be taken to avoid unnecessary duplication.

EFRAG noted that this was an important project and recommended that staff ensure appropriate coverage of the topic on the EFRAG website and in newsletters.

The next Disclosure Framework Advisory Panel meeting will be held at the end of October. A first issues paper on this topic is to be discussed by EFRAG by the end of the year.

## **EFRAG Proactive Project *Business Model***

---

EFRAG and the national standard setters of France (ANC) and the United Kingdom (ASB) are jointly conducting a proactive project on the Business Model. During its October meeting, EFRAG members discussed a paper describing the initial thinking about the scope and direction of the project. No decisions were taken.

## **EFRAG Consultation on proactive work**

---

At its October meeting, EFRAG members also received an update on the status of EFRAG's formal consultation on its proactive work and were asked for their input. No decisions were taken.

### **Future meetings**

The next meetings of EFRAG TEG will take place on 19 October 2010 (by public conference call) and from 8 – 10 November 2010.

The next CFSS meeting takes place on 7 December 2010.