

January 2012

## Summary of EFRAG meetings held in January 2012

From 16 to 18 January 2012, EFRAG held its monthly meeting. The following topics were discussed during the monthly meeting:

- IFRS 10 *Consolidation*, IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities*, IAS 27 *Separate Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* – Discussion of the draft endorsement advices
- IASB Exposure Draft – *Investment Entities* – Final comment letter
- IASB Exposure Draft – *Transition Guidance (proposed amendments to IFRS 10)* – Draft comment letter
- IASB Exposure Draft – *Revenue from Contracts with Customers* – Draft comment letter
- IFRS 13 *Fair Value Measurement* – Final endorsement advice
- Offsetting – Amendments to IAS 32 and Amendments to IFRS 7 – Draft endorsement advice
- IASB Project *Financial Instruments* – An update for EFRAG TEG
- Amendments to IAS 12 – *Deferred Tax: Recovery of Underlying Assets* – Final endorsement advice
- IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* – Final endorsement advice
- Amendments to IFRS 1 – *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* – Final endorsement advice
- IASB Exposure Draft – *Government Loans (proposed amendments to IFRS 1)* – Final comment letter
- EFRAG Proactive project *Disclosure Framework for the Notes to the Financial Statements* – Discussion of risk disclosures
- EFRAG Proactive project *Considering the Effects of Accounting Standards* – Discussion of possible recommendations
- ESMA's consultation paper *Considerations of materiality in financial reporting* – Discussion of draft comment letter

### Highlights

#### **Endorsement Advices**

EFRAG finalised its endorsement advices to the European Commission on IFRS 13 *Fair Value Measurement*, Amendments to IAS 12 *Deferred Tax Recovery of Underlying Assets*, IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* and Amendments to IFRS 1 *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (page 4, 5 and 6, respectively).

*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.

EFRAG also prepared its draft endorsement on Disclosures – Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7) and Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32). The draft endorsement advice will be published on EFRAG’s website next week. Comments on the draft endorsement advice are invited by 26 February 2012.

### **Comment letters**

EFRAG approved its final comment letters on the IASB Exposure Draft *Investment Entities* and the IASB Exposure Draft *Government Loans (proposed amendments to IFRS 1)* (page 3 and 6, respectively).

EFRAG also approved its draft comment letters on the IASB Exposure Draft *Transition Guidance (proposed amendments to IFRS 10)* and the IASB Exposure Draft *Revenue from Contracts with Customers*.

#### IASB Exposure Draft *Transition Guidance* (proposed amendments to IFRS 10)

In its draft comment letter, EFRAG supports the proposed amendments as they provide greater clarity and ensure consistent application of the transition requirements of IFRS 10. Comments are invited by 9 March 2012.

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

In its draft comment letter, EFRAG notes that many of its concerns expressed in relation to the 2010 ED have now been solved. However, EFRAG disagrees with some of the proposals. These proposals include the onerous test at the level of performance obligations and additional disclosures. Comments are invited by 9 March 2012.

## **IFRS 10, IFRS 11 and IFRS 12 - Discussion of the draft endorsement advices**

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During this meeting EFRAG continued to discuss – IFRS 10, IFRS 11, IFRS 12, IAS 27 (amended 2011) and IAS 28 (amended 2011) (the Standards). EFRAG discussed the technical assessment for the endorsement in the EU and its initial assessment of the costs and benefits of the Standards that would arise from their implementation in the EU. EFRAG’s initial assessment is that the standards meet the technical criteria to be adopted in the EU.

However, EFRAG indicated that it would not support the effective date of IFRS 10, which is 1 January 2013. EFRAG arrived at this tentative decision for two distinct reasons. Firstly, the results of the field-tests led by EFRAG confirmed that for some companies, mainly banks and insurers, the effective date of 1 January 2013 leaves them insufficient time to develop a common understanding of how the principles in IFRS 10 should be applied in preparing meaningful and consistent financial reporting.

Secondly, EFRAG noted that the IASB has recently issued the Exposure Draft *Investment Entities* and the IASB Exposure Draft *Transition Guidance (proposed amendments to IFRS 10)*. The amendment to IFRS 10 are only intended to clarify the transition provisions of that standard (less than a year before the standard becomes effective), while the Exposure Draft *Investment Entities* creates uncertainty for constituents in the application of that standard and potentially unnecessary costs.

EFRAG has therefore prepared a draft recommendation that the effective date for IFRS 10 should be 1 January 2014, with early application permitted. As EFRAG recommends that the Standards should be adopted at the same time, the deferral of the effective date is recommended to apply to all.

EFRAG expects to issue in early February 2012 the Invitation to Comment on its draft endorsement advice on IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28.

## **IASB Exposure Draft - *Investment Entities***

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EFRAG finalised its comment letter to the IASB on the Exposure Draft *Investment Entities*, which was published in August 2011.

Whilst EFRAG broadly welcomes the proposal in the ED, it emphasises in its comment letter that a non-investment entity parent should be required to consolidate its investment entity subsidiaries, but that the parent should retain the fair value measurement of the controlled entities that are held through those investment entity subsidiaries.

Furthermore, EFRAG agrees that investment entities should be required to measure their investments in associates as fair value. However EFRAG believes that the option in IAS 28 to measure investments in associates at fair value should be maintained for those mutual funds and other entities that do not meet the characteristics of investment entities and have access to the option today. EFRAG notes that the existing fair value option in IAS 28 did not raise any concerns in the past.

The comment letter is available on EFRAG's website.

## **IASB Exposure Draft - *Transition Guidance (proposed amendments to IFRS 10)***

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EFRAG discussed and approved its draft comment letter to the IASB in response to the Exposure Draft *Transition Guidance (proposed amendments to IFRS 10)* (the ED) which was published in December 2011.

The ED clarifies that the 'date of initial application' means the beginning of the annual reporting period in which IFRS 10 is applied for the first time. The ED also confirms the relief from retrospective application would apply to an investor's interest in investees that were disposed before the date of initial application of IFRS 10.

In its draft comment letter EFRAG welcomes the IASB's decision to clarify the transition guidance in IFRS 10. EFRAG supports the proposed amendments as they provide greater clarity and ensure consistent application of the transition requirements of IFRS 10. EFRAG agrees with the amendment as it provides an appropriate trade-off between the costs to preparers and benefits to users.

The draft comment letter is available on EFRAG's website. The comments on the draft EFRAG comment letter are invited by 9 March 2012.

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

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At its January meeting, EFRAG approved its draft comment letter in response to the IASB ED *Revenue from Contracts with Customers*.

In general, EFRAG welcomes the changes made to the 2010 ED, and notes that many of its concerns expressed in relation to the 2010 ED have been resolved. However, EFRAG disagrees with the proposals to:

- limit the onerous test to performance obligations satisfied over a period of time greater than one year;

- require the onerous test to be performed at a performance obligation level;
- require offsetting of advances received and contract assets in all circumstances;
- require contingent amounts to be allocated to either one or all performance obligations within a contract, but not to a relevant selection of them;
- require a list of specific disclosure requirements in IAS 34 *Interim Financial Reporting*; and
- include only sales-based variable consideration in the special requirements for when to recognise revenue related to licence agreements of intellectual property (paragraph 85 of the ED).

In addition, EFRAG thinks that clarification is needed whether a contract is a contract with a customer or a contract with a partner or collaborator, and on how to distinguish between a right of return, a customer acceptance clause and a put option.

The draft comment letter is available on EFRAG's website. The comments on the draft EFRAG comment letter are invited by 9 March 2012.

## **IFRS 13 Fair Value Measurement**

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In November 2011, EFRAG issued an Invitation to Comment on its draft endorsement advice and a draft Effect Study Report on IFRS 13 *Fair Value Measurement*, which was issued by the IASB in May 2011.

IFRS 13 sets out a single IFRS framework for measuring fair value and provides comprehensive guidance on how to measure the fair value of both financial and non-financial assets and liabilities. IFRS 13 applies when another IFRS requires or permits fair value measurement or disclosures about fair value measurements, thus it does not set out requirements on "when to" measure assets and liabilities at fair value.

EFRAG has issued its Endorsement Advice Letter and Effects Study Report relating to the endorsement of IFRS 13. EFRAG has assessed that IFRS 13 meets the technical criteria for endorsement. EFRAG has also concluded that the benefits to be derived from implementing IFRS 13 are likely to outweigh the costs involved.

## **Offsetting - Amendments to IAS 32 and Amendments to IFRS 7**

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In December 2011, the IASB issued *Disclosures—Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7)* and *Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32)*, which add disclosure requirements for netting arrangements (including rights to set off and similar agreements) and bring clarification to the offsetting criteria, respectively.

In January 2012 EFRAG discussed and concluded, on a preliminary basis, that those amendments meet the technical criteria for endorsement.

EFRAG will be consulting on its initial assessment of the amendments against the technical criteria for the endorsement in the EU and on its initial assessment of the costs and benefits that would arise from the implementation and application of the amendments in the EU.

EFRAG's initial assessment is that both amendments satisfy the technical criteria for EU endorsement and EFRAG should therefore recommend their endorsement.

The comments on the draft EFRAG endorsement advice are invited by 26 February 2012.

## **IASB Project *Financial Instruments***

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EFRAG received an update in relation to the IASB's Exposure Draft *Mandatory Effective Date and Transition Disclosures*, and the latest developments in relation to the Board's deliberations on the limited modifications to IFRS 9 and macro hedge accounting.

EFRAG did not take any decisions at this meeting.

## **Amendments to IAS 12 - *Deferred Tax Recovery of Underlying Assets***

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EFRAG considered the comments received in response to its Invitation to Comment on the 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 finalised and approved its final endorsement advice and effects study report, taking into account the comments received on its Invitation to Comment. EFRAG assessed the Amendments against the technical criteria for endorsement in the EU and has concluded that they meet those criteria. EFRAG has also concluded that the benefits of the Amendments outweigh the costs.

Accordingly, EFRAG has published its Endorsement Advice Letter and Effects Study Report relating to the endorsement of the Amendments on its website.

## **IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine***

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In November 2011, EFRAG issued an Invitation to Comment on its draft endorsement advice and a draft effect study report in respect to IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine*, which was issued by the IASB in October 2011.

Entities engaged in surface mining often need to remove mine waste material ('overburden') to gain access to mineral ore deposits. The removal of such waste material results in a combination of ore and waste (which may contain some usable material) or it could instead allow the access to additional ore body. Waste removal costs that are incurred in surface mining activity during the production phase of the mine are defined as production stripping costs.

IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* provides guidance on recognition of production stripping costs as an asset and the initial and subsequent measurement of the stripping activity asset.

EFRAG assessed IFRIC 20 against the technical criteria for endorsement in the EU and has concluded that they meet those criteria. EFRAG has also concluded that the benefits of IFRIC 20 outweigh the costs.

EFRAG has published its Endorsement Advice Letter and Effects Study Report relating to the endorsement of IFRIC 20 on its website.

## ***Amendments to IFRS 1 - Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters***

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In December 2011, EFRAG issued an Invitation to Comment on its draft endorsement advice and a draft Effect Study Report on the Amendments to IFRS 1 *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (the Amendments), which was issued by the IASB in December 2010.

The Amendments introduce a new exemption in the scope of IFRS 1 *First-time Adoption of International Financial Reporting Standards*. Entities that had been subject to severe hyperinflation are allowed to use fair value as the deemed cost of their assets and liabilities in their opening IFRS statement of financial position. In addition, the Amendments also replace the references to fixed dates in IFRS 1 with references to the date of transition.

EFRAG assessed the Amendments against the technical criteria for endorsement in the EU and has concluded that they meet those criteria. EFRAG has also concluded that the benefits of the Amendments outweigh the costs.

EFRAG has published its Endorsement Advice Letter and Effects Study Report relating to the endorsement of the Amendments on its website.

## ***IASB Exposure Draft - Government Loans (proposed amendments to IFRS 1)***

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In May 2008, the IASB amended IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*, as part of the Annual Improvements Project, in order to require government loans with a below-market rate of interest to be measured at fair value on initial recognition. The IASB required applying the amendments prospectively to new loans in order to avoid fair value measurements at a past date.

In September 2011, the IASB decided to amend IFRS 1 in order to allow first-time adopters of IFRSs the same prospective application of the provision set out in IAS 20. Consequently, the IASB published on 19 October 2011 the Exposure Draft *Government Loans* (proposed amendments to IFRS 1) (the ED). The ED proposes to allow first-time adopters to apply the amendments retrospectively if the information needed to comply with IAS 20 requirements was obtained at the time of initial recognition of the loan.

In November 2011, EFRAG issued its draft comment letter and based on the comments received, EFRAG finalised its final comment letter in response to the IASB Exposure Draft.

In its final comment letter, EFRAG is supportive of what the proposals are trying to achieve. However, EFRAG believes that the Board should provide guidance on the recognition and measurement of all government loans existing at the date of transition, and not just on those that were recognised as liabilities under previous GAAP.

Finally, EFRAG supports the option for retrospective application as it increases the relevance and the comparability of financial information, but it believes the Board should require entities that elect to use this option apply it consistently to all government loans for which the information needed is available.

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

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EFRAG debated the role and extent of disclosures around risk and whether disclosures about risk should be included in the notes to the financial statements.

Risk is a pervasive concept, that may be used to refer to different items such as measurement uncertainty at the reporting date or exposure to changes in future economic conditions; information on risk may range from measuring the exposure at the reporting date to an explanation of risk management techniques and processes within the entity.

EFRAG acknowledged that information about risk was an important aspect of what should be disclosed in the notes, however it was not apparent where the boundary should be drawn between risk information relevant to the financial statements and more general information about risk. There was consensus about including information around measurement uncertainty at the reporting date. Staff was asked to undertake further research on where the boundary between the notes and other parts of the annual report could be drawn.

## ***EFRAG Proactive Project Considering the Effects of Accounting Standards***

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EFRAG started to discuss its recommendations relating to the issues raised in the Discussion Paper *Considering the Effects of Accounting Standards* (the DP), which was published in January 2011 by EFRAG and 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.

In formulating its position on the different aspects of accounting standards' effects analysis, EFRAG took into consideration the outcome of the public consultation (31 comment letters have been received to the DP and several meetings have been held). EFRAG will continue the discussion on its next meetings and will issue a feedback statement in the due course. The UK ASB is debated the same issues in parallel and EFRAG and the UK ASB expect to be able to jointly publish a common position.

## ***ESMA's report Considerations of materiality in financial reporting***

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In November, ESMA issued its consultation paper *Considerations of materiality in financial reporting*. In this paper, ESMA argues that there are different views regarding the practical application of materiality among preparers, auditors, possibly users and in some instance regulators.

EFRAG noted that the application of materiality is first and foremost an issue of professional judgment. Materiality should be judged based on specific facts and circumstances, and the assessment should not be based on strictly quantitative rules or thresholds. EFRAG agrees that there is room for improvement in the

application of materiality, especially in relation to disclosures, to ensure that preparers provide all material information and avoid cluttering financial statements with immaterial information.

EFRAG expressed the view that regulators should not issue guidance on the application of materiality. EFRAG is of the view that it is the IASB's role to clarify concepts in IFRS such as materiality and promote consistent application of those concepts.

EFRAG expects to finalise its draft submission on the consultation paper in a conference call.