Draft Endorsement Advice on Annual Improvements to IFRS Standards 2015-2017 Cycle
Cover Note

Objective

1 The objective of the session is to discuss, and agree to recommend to the EFRAG Board, a draft endorsement advice on the *Annual Improvements to IFRS Standards 2015-2017 Cycle* ('the Amendments') published by the IASB on 12 December 2017.

Agenda papers

2 In addition to this cover note, agenda papers for this session are:

(a) Paper 08.02 – EFRAG's Draft Letter to the European Commission;

(b) Paper 08.03 – Invitation to Comment on EFRAG's Draft Letter to the European Commission; and

(c) Paper 08.04 – Annual Improvements to IFRS Standards 2014-2016 Cycle. For background.

The Amendments

3 The Amendments comprise clarifications of the following issues:

(a) Issue 1 - IFRS 3 *Business Combinations and* IFRS 11 *Joint Arrangements: Previously held interest in a joint operation*;

(b) Issue 2 - IAS 12 *Income Taxes: Income tax consequences of payments on financial instruments classified as equity*;

(c) Issue 3 - IAS 23 *Borrowing Costs: Borrowing costs eligible for capitalisation*.

Issue 1 - IFRS 3 Business Combinations and IFRS 11 Joint Arrangements:

4 The amendment to IFRS 3 clarifies that a transaction of obtaining control of a business that is a joint operation, is a business combination achieved in stages and the acquirer should apply the relevant requirements of IFRS 3, including remeasuring of the entire previously held interest in the joint operation.

5 The amendment to IFRS 11 clarifies that the acquirer should not remeasure the previously held interest in transactions of obtaining joint control of a business that is a joint operation.

6 An entity shall apply those amendments to business combinations, or transactions in which it obtains joint control, for which the acquisition date, or transaction date, is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019. Earlier application is permitted.

Issue 2 – IAS 12 Income Taxes: Income tax consequences of payments on financial instruments classified as equity

7 The amendment to IAS 12 clarifies that the income tax consequences of payments on financial instruments classified as equity should be recognised according to where the past transactions or events that generated distributable profits have been recognised.

8 An entity shall apply those amendments for annual reporting periods beginning on or after 1 January 2019 with earlier application permitted. The amendments apply to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period of the annual reporting period in which the entity first applies those amendments.

Issue 3 – IAS 23 Borrowing Costs: Borrowing costs eligible for capitalisation

9 The amendment to IAS 23 clarifies that, when substantially all the activities necessary to prepare a qualifying asset for its intended use or sale, an entity treats any outstanding borrowing made specifically to obtain that qualifying asset, as part of the funds that it has borrowed generally.

10 An entity shall apply those amendments for annual reporting periods beginning on or after 1 January 2019 with earlier application permitted. The amendments apply to borrowing costs incurred on or after the beginning of the annual reporting period in which the entity first applies those amendments

Exposure Drafts and EFRAG's Comment Letters

11 The amendments regarding Issue 1 were issued in draft form on 28 June 2016 in Exposure Draft ED/2016/1 *Definition of a Business and Accounting for Previously Held Interests*, which comprised two issues. However, in September 2017, the IASB decided to include the one related to joint arrangements to Annual Improvements Project cycle 2015-2017, and to proceed with the amendment regarding definition of a business separately.

12 In its comment letter issued on 9 November 2016, EFRAG supported the IASB's proposals to clarify the accounting for previously held interests in a joint operation.

13 The amendments regarding Issue 2 and 3 were issued in draft form on 12 January 2017 in Exposure Draft ED/2017/1 *Annual Improvements to IFRS Standards 2015-2017 Cycle*, which comprised three amendments. However, in May 2017, the IASB decided to separately proceed with the amendment related to IAS 28 *Investments in Associates and Joint Ventures: Long-term interests in an associate*.

14 On 19 April 2017, in its comment letter on ED/2017/1, EFRAG broadly agreed with most of the proposals.

15 However, EFRAG was concerned that amending IAS 12 without providing guidance on how to determine whether payments are distributions of profits might not lead to a significant improvement in consistent application compared to the current situation. The IASB, in the Basis for Conclusion considered that request and explained that the amendments were not intended to change what is and is not a distribution of profits and they simply clarify the requirements of paragraph 57A. Including indicators or requirements that distinguish distributions of profits from other distributions would go beyond the scope of the amendments. Furthermore, any attempt to define or describe distributions of profits could affect other IFRS Standards and IFRIC Interpretations, what would risk unintended consequences.

16 Regarding the transition requirements, EFRAG agreed that the proposals should be applied prospectively.

Questions to EFRAG TEG

17 Do you approve the draft endorsement advice for forwarding to the EFRAG Board for approval by written procedure?

18 Do you approve the invitation to comment for forwarding to the EFRAG Board for approval by written procedure?