

July 2011

### Summary of an EFRAG meeting held in July 2011

From 13 to 15 July 2011, EFRAG held its monthly meeting and discussed the following:

- IASB's new standards related to *Consolidation* project – IFRS 10 *Consolidation*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities*
- IAS 19 *Employee Benefits* (as revised in 2011)
- Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income*
- IASB Exposure Draft *Improvements to IFRSs 2009-2011*
- IASB re-deliberations in the project *Leases*
- IASB re-deliberations in the project *Financial Instruments*
- IASB re-deliberations in the project *Insurance Contracts*
- IASB re-deliberations in the project *Revenue from Contracts with Customers*
- IASB project *Investment Entities*
- IASB Agenda Consultation
- IFRS for SMEs – Q&A procedure
- EFRAG Proactive project *Business Combinations under Common Control*
- EFRAG Proactive project *Disclosure Framework for the Notes to the Financial Statements*
- EFRAG Outreach on *Financial Statements Presentation*.

### Highlights

#### *Endorsement advice*

EFRAG finalised its draft endorsement advice and a draft effects study report on IAS 19 *Employee Benefits*, as revised in 2011, and on the Amendments to IAS 1 *Presentation of Items of Comprehensive Income*. EFRAG is seeking comments from constituents on these drafts. The comment deadline is 23 September 2011 (page 2 and 3, respectively).

## Comment letter to the IASB

EFRAG finalised its draft comment letter to the IASB on the Exposure Draft *Improvements to IFRSs 2009-2011* (the ED). The draft comment letter supports the amendments proposed in the ED, however recommends bringing further clarifications to IAS 12 in respect of taxes on distribution to owners. EFRAG is seeking comments from constituents on this draft. The comment deadline is 30 September 2011 (page 3).

## IASB's new standards related to *Consolidation* project

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EFRAG discussed IFRS 10 *Consolidation*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosures of Interests in Other Entities*, in view of its initial assessment of the new requirements on consolidation and joint arrangements against the technical criteria for the endorsement in the European Union.

The aspects of the new standards discussed at the meeting included: the definition of control; the concept of relevant activities; *de facto* control; power without a majority of voting rights; potential voting rights; agent versus principal relationship; consolidation of special purpose entities; accounting for different types of joint arrangements; and transitional requirements of the standards.

EFRAG received an update on the feedback collected by EFRAG staff during its consultative meetings with various groups of constituents. EFRAG considered whether it required any additional input from constituents for its initial assessment of the new requirements on consolidation and joint arrangements, and the best approach to collect that input. EFRAG tentatively decided to involve European national standard setters in the additional consultation process. As part of its initial assessment, EFRAG will also consider effects studies on the standards prepared by the IASB's staff, which are expected to be issued shortly.

EFRAG will proceed with its initial assessment of the new standards against the technical criteria for endorsement in the European Union at its future meetings.

## IAS 19 *Employee Benefits* (as revised in 2011)

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In June 2011, the IASB issued a revised version of IAS 19 *Employee Benefits* (IAS 19 (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.

EFRAG completed its initial assessment of IAS 19 (2011) against the EU endorsement criteria and completed an initial study of their cost and benefits. EFRAG's initial assessment is that IAS 19 (2011) meets the criteria for endorsement in the EU and the benefits that are expected to arise from the amended standard are likely to exceed the cost in implementing it. EFRAG is inviting comments on its draft endorsement advice and a draft effects study report, which are both available on EFRAG's website. The comment deadline is 23 September 2011.

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

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In June 2011, the IASB issued Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income* (the Amendments). 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.

EFRAG completed its initial assessment of the Amendments against the EU endorsement criteria and completed an initial study of their cost and benefits. EFRAG's initial assessment is that the Amendments meet the criteria for endorsement in the EU, and the benefits that are expected to arise from the Amendments are likely to exceed the cost in implementing them. EFRAG is inviting comments on its draft endorsement advice and a draft effects study report, which are both available on EFRAG's website. The comment deadline is 23 September 2011.

## IASB Exposure Draft *Improvements to IFRSs 2009-2011*

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EFRAG discussed its draft comment letter for the IASB on the 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.

The draft comment letter supports the amendments proposed in the ED. However, suggests 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 draft comment letter is available on EFRAG's website. The comment deadline is 30 September 2011.

## IASB re-deliberations in the project *Leases*

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EFRAG discussed the proposed definition of a lease and the refined guidance on identifiable assets and the right to control the use of the asset throughout the lease term.

EFRAG also considered whether the IASB should identify additional or alternative criteria to define a lease. Amongst other criteria, EFRAG discussed the exposure to capacity risk, variability of lease payments for changes in market prices and exemptions for non-depreciable assets.

EFRAG made a number of comments and suggestions for improving the guidance; however, it did not express clear support for any alternative criteria.

EFRAG will continue to follow closely the IASB's re-deliberations.

## IASB re-deliberations in the project *Financial Instruments*

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EFRAG received an update on the latest developments in relation to the IASB *Financial Instruments* project, including the IASB's and the FASB's joint re-deliberations in respect of offsetting of financial assets and financial liabilities, and impairment of financial assets; the IASB's re-deliberations in respect of general hedge accounting; and the FASB's deliberations in respect of classification and measurement of financial instruments.

EFRAG did not take any decisions at this meeting.

## IASB re-deliberations in the project *Insurance Contracts*

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EFRAG received an update on the IASB's re-deliberations of the proposals included in the Exposure Draft *Insurance Contracts* (the ED). EFRAG also received an update on the discussion held at the EFRAG Insurance Advisory Working Group on 21 June 2011. The following topics were discussed:

- *Unlocking of the residual margin* – EFRAG discussed the arguments considered by the IASB in arriving at its tentative decision to adjust the residual margin for changes in estimates. As the unlocking of the residual margin is related to the reported volatility, EFRAG noted that the IASB should consider the overall effect of different alternatives for addressing the volatility issue and the interaction with other standards.
- *Presentation of the statement of comprehensive income* – EFRAG discussed three different alternatives for the presentation of the income statement, which were developed by the IASB staff. EFRAG made various comments on the alternative models, but did not express a preference for any of them.
- *Reinsurance* – EFRAG considered the IASB's tentative decisions in relation to the reinsurance proposals, including the accounting for upfront gains or losses arising on entering into a reinsurance contract. EFRAG did not form a view on the tentative decisions.

EFRAG will continue to follow closely the IASB re-deliberations on this project.

## IASB re-deliberations in the project *Revenue from Contracts with Customers*

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EFRAG considered the scope, extent and timing of the European field-testing of the revised proposals on *Revenue from Contracts with Customers*. The revised proposals are expected to be published by the IASB for public comment in the third quarter of 2011 with a comment period of 120 days. The objective of the field-testing will be to collect input in relation to the implementation of the revised proposals and their application in practice.

EFRAG has tentatively decided that the field-testing should focus on the following topics:

- *Determining separate performance obligations and allocating consideration* – defining separate performance obligations in a multiple element contract, interpreting the notion of integration service, allocating consideration to separate performance obligations using different methods
- *Timing of revenue recognition* – testing the criteria for determining if a performance obligation is satisfied over time (PoC), accounting for royalties, estimating the costs of implementing and applying the proposals
- *Time value of money* – application under the percentage of completion accounting and to contracts with multiple performance obligations
- *Disclosures* – assessing costs and benefits of the disclosure requirements and
- *Effective date and transition requirements.*

EFRAG has tentatively decided to conduct the field-testing in cooperation with the IASB and the European national standard setters, and to make a public call for participants. The field-testing will focus specifically on the telecommunications, software, pharmaceutical, utilities industries, and on the companies operating under long-term contracts (e.g. construction and engineering).

Once the preliminary arrangements are finalised, EFRAG will announce the field-testing and will issue a call for participants on its website.

## IASB project *Investment Entities*

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EFRAG discussed the forthcoming proposals on the IASB project *Investment Entities*, which are expected to be issued for public comment in the coming weeks. The discussion focused on the definition of investment entities, which are expected to be in the scope of the exception to the consolidation requirements. Such entities are expected to be required to measure their controlled investments at fair value.

EFRAG was generally supportive of an exception to the consolidation requirements; however, expressed some comments in relation to *when* and *how* such exception should be applied.

EFRAG noted that one of the key criteria for meeting the definition of an investment entity was the requirement to have an exit strategy and to generate returns from capital appreciation. It is expected that the proposals will not include ‘bright lines’ for defining a specified term in relation to an exit strategy, and some EFRAG members supported this approach.

EFRAG also expressed concerns that a parent of an investment entity would be prohibited from retaining fair value accounting, if that parent was not an investment entity itself. EFRAG noted that the IASB had not provided sufficiently convincing arguments for prohibiting the ‘roll-up’ of the fair value accounting.

EFRAG will discuss its draft comment letter to the IASB once the exposure draft is published.

## IASB Agenda Consultation

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EFRAG members discussed the forthcoming IASB agenda consultation with a view of providing input to the EFRAG Planning and Resource Committee that will be approving the comment letter to the IASB on EFRAG’s behalf. The IASB is planning to request views on its agenda in the third quarter of 2011.

## IFRS for SMEs - Q&A procedure

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EFRAG considered the draft Questions and Answers about IFRS for SMEs (Q&A) published by the IFRS Foundation's SME Implementation Group. EFRAG expressed concerns about the number of Q&A that would be issued. It was noted that instead of focusing on a few pervasive issues in developing the draft Q&A, the SME Implementation Group was about to create a rule-oriented environment with extensive amount of additional literature.

## EFRAG Proactive project *Business Combinations under Common Control*

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EFRAG received an updated version of the revised staff draft of the discussion paper on Accounting for Business Combinations under Common Control (the DP). The purpose of the session was to finalise the DP, if possible, and agree on the next steps to ensure that the DP is issued to constituents in the near future.

EFRAG expressed mixed views on the draft DP. While there was general support for the overall content and structure of the draft DP, there were suggestions for improvement in some other areas.

EFRAG gave the final directions to staff in order to have the next draft of the DP completed by mid-August for a decision on the DP to be made in the first week of September 2011.

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

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Following the discussion at the June meeting, EFRAG continued the analysis of the purpose of the notes to the financial statements. In particular, EFRAG discussed *when* and *what* type of information should be disclosed about transactions and other events that did not result in the recognition of assets and liabilities at the balance sheet date.

EFRAG noted that the description of the purpose of the notes should also recognise their role in allowing users to assess the management's stewardship.

EFRAG did not support the notion that certain information should be disclosed regardless of its materiality only for the purpose of improving comparability.

EFRAG acknowledged that there are other organisations working on similar projects, but confirmed the importance of the project for its proactive agenda, and that it was likely to complement these other activities.

## EFRAG Outreach on *Financial Statements Presentation*

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EFRAG reviewed comments received from European constituents on a Paper *Financial Statement Presentation* (the Paper), which was issued for public comment in October 2010. The Paper was published as part of the European outreach activities in relation to the tentative decisions included in the IASB's staff draft of the exposure draft *Financial Statement Presentation* (the Draft ED) and was based on EFRAG's

preliminary views. Although the work on the *Financial Statement Presentation* project had to be postponed by the IASB due to commitments to finalise other projects with a higher priority, EFRAG has decided to conclude its outreach activities, which were initiated prior to changes in the project timetable, in order to provide the IASB with a complete set of European views on this project. During the European outreach, constituents were invited to provide their views in meetings organised in cooperation with the European National Standard Setters, via an online questionnaire and by responding to the Paper. EFRAG reported on the feedback received during the meetings with constituents and via the online questionnaire in February 2011.

In addition to input received from constituents during the meetings and via the online questionnaire, EFRAG has received seven comment letters, and one note, on the discussion with the IASB staff on the respective issues in response to the Paper. The respondents to the Paper shared the majority of EFRAG's preliminary views on the Draft ED, and their comments were consistent with the feedback received during the meetings with the European constituents.

EFRAG has issued a letter to the IASB on the comments on the Paper. The letter complements the feedback on the meeting with European constituents published in February 2011, and completes the overall picture of the European views on the IASB's tentative decisions in respect to the Financial Statement Presentation project. The letter to the IASB is available on EFRAG's website.