EFRAG

European Financial Reporting Advisory Group

18 February 2013

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir/Madam,

Re: Exposure Draft *Annual Improvements to IFRSs 2011–2013 Cycle*

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Exposure Draft, *Annual Improvements to IFRSs 2011 – 2013 Cycle,* issued by the IASB on 20 November 2012 (the 'ED').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of the definitive IFRS in the European Union and European Economic Area.

Our detailed comments and responses to the questions in the ED are set out in the appendix. To summarise we agree with most proposals in the ED and with the objective they are trying to achieve but EFRAG is concerned about the issues explained below.

EFRAG agrees with the amendment to IAS 40, which provides a short-term solution. However, the amendment leaves unaddressed broader issues – such as whether a single investment property is a business and the need for similar amendments to other standards (e.g. IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*) – that should be considered as part of the post-implementation review of IFRS 3.

EFRAG agrees with the proposed amendment to IFRS 1 on the basis that it may reduce the diversity in practice and that dropping the issue at this stage might, in fact, create confusion. Nevertheless, we believe that in the future similarly minor issues should not result in an amendment to the standards or the Basis for Conclusions.

In addition, EFRAG believes that the IASB should refrain from making amendments to the bases for conclusions of standards, unless it wishes to correct outright errors. In our view, amendments to bases for conclusions cannot take the place of actual standard setting. Furthermore, we would like to note that such amendments do not form part of the standards themselves and hence do not affect IFRSs as endorsed in the European Union.

If you would like to discuss our comments further, please do not hesitate to contact Giorgio Acunzo or me.

Yours sincerely,

Françoise Flores
EFRAG Chairman

APPENDIX 1

EFRAG's responses to the questions raised in the ED

Question 1
Do you agree with the IASB's proposal to amend the Standard as described in the exposure draft? If not, why and what alternative do you propose?

Question 2
Do you agree with the proposed transitional provisions and effective date for the issue as described in the exposure draft? If not, why and what alternative do you propose?

1 EFRAG understands that the annual improvement process offers a valuable opportunity to change current standards in order to address – on a timely basis – issues raised by constituents of widespread concern and urgency. Therefore, EFRAG agrees that most of the issues addressed by the IASB within the Exposure Draft *Annual Improvements to IFRSs 2011 – 2013 Cycle* ('the ED') meet the criteria of the IASB Due Process Handbook and therefore they should be resolved as part of the annual improvement project.

2 However, EFRAG notes that the proposed amendment to the basis for conclusions in IFRS 1 appears to be minor; therefore EFRAG is concerned about the purposes for which the annual improvement exercise is currently being used.

3 EFRAG believes that changing the standards bears a cost and therefore IFRSs should only be amended where there is a compelling case to do so and the benefits to be gained outweigh the costs.

4 Furthermore, EFRAG regrets that the IASB is systematically proposing amending the basis for conclusions of the standards to address the issues raised by constituents instead of improving the text within the standards. In fact, EFRAG notes that the basis for conclusions should contain, according to paragraph 3.76 of the proposed new edition of the IASB and IFRS Interpretations Committee Due Process Handbook (issued in May 2012) only '*the rationale for why* (the IASB) *made the decisions it reached in developing or changing an IFRS. The Basis for Conclusions also includes the IASB's responses to comments received when the proposals were exposed*'.

Issue 1: IFRS 1 – First-time Adoption of International Financial Reporting Standards: Meaning of effective IFRSs

EFRAG agrees with the proposed amendment. However, EFRAG believes that in the future similarly minor issues should not result in an amendment to the standards or the Basis for Conclusions.

5 EFRAG believes that changes to standards and changes to the basis for conclusions bring with them standard setting costs for the IASB and due process costs for its constituents. Therefore such changes should only be made if there is a compelling case to do so. Although we believe that IFRS 1 is already sufficiently clear, we support the amendment on the basis that it may reduce the diversity in practice and that dropping the issue at this stage might, in fact, create confusion. Nevertheless, EFRAG believes that in the future similarly minor issues should not result in an amendment to the standards or the Basis for Conclusions.

6 EFRAG further notes that amendments to the basis for conclusions of IFRS 1, which is intended as a record of the IASB's thinking at the time a standard is issued, will not affect IFRS as endorsed in the European Union.

7 Finally, EFRAG understands that the IASB has not included an effective date because the proposed amendments only aim to clarify the basis for conclusions in IFRS 1.

Issue 2: IFRS 3 – Business combinations: Scope of exception for joint ventures

EFRAG agrees with the proposed amendments.

8 EFRAG agrees with the IASB's assessment of the issues and with its proposed amendments to address them.

Issue 3: IFRS 13 – Fair Value Measurement: Scope of paragraph 52 (portfolio exception)

EFRAG welcomes the proposal to clarify that the scope exception applies to all contracts within the scope of IAS 39 and IFRS 9.

9 EFRAG welcomes the amendments as we believe they clarify that the scope of the measurement exception in IFRS 13 includes all financial instruments as defined in the relevant standards.

10 However, while agreeing with the proposal of linking IFRS 13 with relevant standards dealing with financial instruments, EFRAG believes that the proposed wording of the basis for conclusions should be improved.

11 EFRAG believes that 'some contracts to buy or sell a non financial item that can be settled net in cash or another financial instrument', defined under paragraph AG 20 of IAS 32, could be in circumstances scoped out from IAS 39 and IFRS 9. Therefore these contracts would also be outside the scope of the proposed amendments.

12 Finally, EFRAG agrees that this amendment should be applied retrospectively.

Issue 4: IAS 40 – Investment Property: Acquisition of investment property: interrelationship with IFRS 3

EFRAG agrees that the amendment provides a short-term solution, but believes that it leaves unaddressed several broader issues that should be considered as part of the post-implementation review of IFRS 3.

13 EFRAG agrees with the IASB's assessment of the issue and with the proposed amendment, which provides a short-term solution. However, the amendment leaves unaddressed broader issues – such as whether a single investment property is a business and the need for similar amendments to other standards (e.g. IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*) – that should be considered as part of the post-implementation review of IFRS 3.

14 However, EFRAG believes that the amendments should be applied retrospectively as it believes that the purchase price allocation accounting within IFRS 3 produces more relevant information for users. In EFRAG's view, it is likely that entities that purchased an investment property had already collected relevant information on the fair value of the asset. Therefore, EFRAG believes that the risk of using hindsight in these circumstances is limited and outweighed by the benefit of having comparable and relevant information.

15 Furthermore, EFRAG understands that the objective of these amendments is to provide clarification on how current guidance in IAS 40 and IFRS 3 already applies. Accordingly, we do not see the need for prospective application of these amendments.

16 Therefore, if retrospective application is to be pursued, EFRAG believes that the IASB should carefully explain in its effects analysis how it considered the costs and benefits of this requirement, and why the use of hindsight would not be of concern in this particular case.

17 Finally, EFRAG notes that while this particular amendment is fairly insignificant in its own right, it points at a much more substantive unaddressed issues resulting from the following significant difference in the accounting for asset acquisitions and business combinations, which include among others:

(a) Treatment of transaction costs should be expensed in business combinations, but should be capitalised for asset acquisitions;

(b) Deferred tax should be recognised in business combinations, but the initial recognition exemption in IAS 12 applies to asset acquisitions;

(c) Treatment of purchase consideration paid in shares – IFRS 3 provides guidance in the case of business combinations, but IFRS 2 applies to all other types of transactions;

(d) Treatment of contingent consideration, which is only defined by IFRS 3 but which is undefined for asset acquisitions; and

(e) Disclosures.

18 EFRAG believes that the IASB should consider the consequences of the distinction between acquisition of assets and businesses as part of the post implementation review of IFRS 3 rather than as part of a series of separate standard setting initiatives, which currently include the following:

(a) IASB projects on:

(i) Accounting for Contingent Consideration in a Business Combination within the Annual Improvements to IFRSs 2010 – 2012 Cycle;

(ii) Scope of application of IFRS 3 and IAS 40, which this annual improvement ED addresses;

(iii) Sales or contributions of assets between an investor and its associate/ joint venture (Proposed amendments to IFRS 10 and IAS 28); and

(iv) Acquisition of an interest in a joint operation (Proposed amendments to IFRS 11);

(b) IFRS Interpretations Committee projects on:

IAS 16, IAS 38 and IFRIC 12 – Variable payments for the separate acquisition of PPE and intangible assets.