

June 2011

**EFRAG - IASB Joint Meeting
held on 14 June 2011****Summary of main messages expressed by the EFRAG delegation**

EFRAG and IASB had one of their regular joint public meetings on 14 June 2011. The EFRAG delegation was composed of the EFRAG Chairman (Françoise Flores), the vice-Chairman of EFRAG TEG (Mike Ashley), the Chairmen of the ANC (Jérôme Haas), GASB (Liesel Knorr) and of the ASB (Roger Marshall) and the vice-Chairman of the OIC (Alberto Giussani), accompanied by their technical directors or a member of their Boards.

IASB was represented by Ian Mackintosh, Vice-Chairman-elect, Elke König, Stephen Cooper, Philippe Danjou, Pat Finnegan, Pat McConnell, Wei-Guo Zhang, Tatsumi Yamada, Warren McGregor, IASB members, and Alan Teixeira, IASB Director of Technical Activities and various staff members responsible for the different projects discussed during the meeting.

Revision of the IASB work programme and publication of near final drafts

EFRAG commends the IASB for having agreed with the FASB a revised schedule for the completion of the active joint projects, including joint efforts towards completing a converged standard on financial instruments.

EFRAG welcomes also the prospect of the publication of staff drafts or near final drafts of the standards prior to publication. EFRAG believes that this supplementary step in the IASB due process provides a desirable opportunity for constituents to check whether the near final requirements are easily understandable and can be implemented in practice without unreasonable cost or difficulty. To make this step fully profitable, the complete set of documents should be made available (draft standard, illustrative examples, basis for conclusions). Some believe that the effect study report should be available as well.

To be efficient the timetable for this supplementary step must be clearly defined – with a clear deadline for possible comments to be made to the IASB– European constituents expect a full three month period to fully consider the operational implications of the near final standards.

EFRAG also believe that this new consultation step should be an opportunity to carry out focused field testing of the requirements which have been identified at comment letter stage as potentially critical in practice. EFRAG wishes to coordinate with the IASB to organise the appropriate field testing exercises.

In the longer term, EFRAG recommends that this supplementary consultation step (publication of a near final draft) become a regular due process step for other than trivial amendments to existing standards. EFRAG recommends also that no final standard be published prior to the related effect studies being ready for publication.

Revenue Recognition and Leases

One of the main objectives of this joint meeting is to discuss with the IASB the results from the joint EFRAG – NSS outreach events that were held in Europe in May, in close coordination with the IASB. EFRAG is grateful to the IASB for having participated in those events, firstly in helping EFRAG shape the relevant material for the events (presentation and summaries of the decisions to date) and secondly in delegating IASB members and staff to participate in the events. This initiative has been very well received by European constituents. A feedback statement summary (as well as detailed notes per event) has been published on the EFRAG website.

Revenue Recognition

While most constituents remain unconvinced that IFRS existing standards on revenue recognition were in need of a complete overhaul, most of them welcome the outcome of most IASB re-deliberations and acknowledge the IASB's willingness to solve concerns raised in the consultation phase.

There remain however two main concerns that EFRAG encourages the IASB to revisit prior to completion of the project:

- the pre-final guidance to continuous transfer of benefits to customers can as presently drafted lead to revenue being recognised even though the entity is not entitled to a corresponding right to payment; also the “no alternative use” criterion does not seem to encapsulate any distinctive economic feature that would justify its prominence in the guidance; as a result, EFRAG has prepared a possible alternative to be discussed at the meeting;
- EFRAG recommends that the issues raised by particular industries (Telecommunications, Software...) be solved prior to the completion of the standard.

In addition to the two main issues above, EFRAG is happy to offer the following comments:

- EFRAG welcomes simplifications decided for the treatment of the time value of money. However, and although the complete exemption has been welcome by European constituents, EFRAG believes that assessing whether there is a significant financing component in short term receivables is not necessarily so burdensome as to justify the total exemption decided by both Boards;
- The IASB should ensure, in this project as in other active projects, that disclosure requirements are moving away from a prescriptive list of information to mandating that information be shaped to the particular circumstances and operations of an entity;
- Were the Board to consider a partial re-exposure, EFRAG recommends that the revised requirements subject to re-exposure be accompanied by the full draft standard, illustrative examples and basis for conclusions.

EFRAG would like to stress that in a number of locations participants noted that the direction taken by the IASB in the re-deliberations on the project deviated significantly from the original proposals; and therefore, argued for the re-exposure of the proposals.

Leases

European constituents have in the course of European outreach events expressed the very strong message that they would prefer the IASB to maintain IAS 17 in its current state or work on marginal improvements. This message has been supported by National Standard Setters who were represented at the EFRAG Consultative Forum of Standard Setters meeting on 8 June.

EFRAG does not believe that the IASB can finalise its project without a fundamental rethink and a full consultation process.

The reason for such strong statements is that the rationale for undertaking the project – all financing liabilities should be recognised on the balance sheet – cannot support a decision to account for all arrangements meeting the revised definition of a lease, irrespective of whether they are financing transactions or arrangements of a different nature. All European constituents who participated in EFRAG outreach events acknowledge, as the Board has done, that arrangements meeting the existing definition of a lease are of two different economic natures. EFRAG agrees with that view also.

As a result, EFRAG recommends the IASB not to pursue the project without reconsidering how to identify leases so as to exclude from the right of use model arrangements which are not financing transactions. While the right of use model is acknowledged as appropriate for transactions which are financing transactions, the arrangements which are encompassed in the definition (either proposed or tentative) and which are not financing transactions should be dealt with as service arrangements, i.e. remain off balance sheet.

Apart from this major and fundamental issue, most of the outcome of the IASB re-deliberations is welcome. More particularly the revision of the definition of a lease is deemed to be a significant improvement. However, most European constituents believe that the IASB should require that only non-genuine options be recognised (a requirement that would be consistent with the decision made on contingent lease payments). Also, an exemption from the right of use model for short term leases should be available.

Insurance Contracts

EFRAG welcomes progress made by the IASB in the project so far. We however wish to highlight the following recommendations:

- EFRAG encourages the IASB to further investigate how the use of OCI could help solve the “volatility issue” in the income statement, while adopting a current value measurement for the insurance contract liability;
- The status of the insurance project should be clearly determined. It is either a joint project with the FASB – and as a result deliberations should be coordinated until final publication – or it is not. If it is not a joint project, the IASB should finalise the project taking account of the views of all possible constituents and publish the final standard without raising any expectations that it might be amended as a result of the outcome of any future deliberations by the FASB;
- EFRAG has advocated in the past that the interrelationships between IFRS 4 and IFRS 9 be fully considered before both standards are finalised; as a result, the IFRS 4 completion timeframe should be aligned with the completion of IFRS 9 final classification and measurement requirements, i.e. after

convergence efforts with the FASB have taken place; as a consequence, EFRAG believes the FASB should be encouraged to finalise its position on insurance contract accounting in the same time frame. EFRAG notes indeed that an IFRS standard on insurance contracts remains urgently needed and should not be delayed for too long;

- EFRAG reiterates its view that the residual margin should be a floating margin;
- EFRAG reiterates its recommendations for the presentation of the performance of an insurance contract activity.

Financial Instruments

Hedge Accounting

Bearing in mind the latest decisions made by the IASB, EFRAG wishes to highlight that denying hedge accounting for sub-Libor instruments triggers a significant concern and to gain visibility on the timing of the consultation and finalisation of macro-hedging requirements. EFRAG reiterates that in its view no final requirements for micro-hedge accounting should be published prior to macro-hedging requirements being finalised.

Offsetting

EFRAG was very supportive of the approach that the Board had taken. The current re-deliberation appears to be reconsidering a number of very fundamental points and risks reopening/repeating much of the debate that the Boards have had already.

Impairment

Development of an improved impairment model for financial assets is crucial. We are, however, somewhat concerned about the rather circuitous road that the Board appears to be taking in achieving this goal. In particular, the publication of an ED, followed by a Supplementary Document and now followed by discussion about a new three-bucket approach makes it increasingly difficult to follow the project and see the wood for the trees.

Consolidation “package”

With IFRS 10, 11 and 12 and the amendments to IAS 27 and IAS 28 being now published, EFRAG is preparing to fulfil its duties as part of the European Union endorsement process.

EFRAG wishes to highlight the following two issues:

- To avoid any duplication of effort, EFRAG wishes to rely on the IASB effect studies that the IASB expects to publish soon. However with an effective date for the new standards set on 1st January 2013, no time should be wasted by EFRAG in carrying out the necessary assessments of the final standards. Voices are starting to be heard in Europe that entities are not granted enough time to understand and implement – with full comparative information – the new standards;
- IFRS 12 requires new disclosures to be presented while the IASB is about to launch the consultation on an exemption from consolidation for venture capital entities. Also the revised consolidation requirements in IFRS 10 may require venture capital entities to re-examine the basis on which they consolidate other entities under the existing standards. EFRAG wishes to understand the timing in which the IASB operates so as to avoid imposing on entities the burden of potentially changing accounting treatments and/or preparing new disclosures that they would abandon soon thereafter.