

February 2011

Summary of EFRAG meetings held in January – February 2011

On 28 January 2011, EFRAG held meetings by public conference call to discuss:

- The IASB's Request for Views on *Effective Dates and Transition Methods*
- EFRAG Outreach Activities on *Financial Statement Presentation*

On 8, 10, and 11 February 2011, EFRAG held its monthly meeting and discussed the following:

- IASB supplementary document to Exposure Draft *Financial Instruments: Impairment*
- IASB Amendments to IFRS 1 *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters*
- IASB Exposure Draft *Offsetting Financial Assets and Financial Liabilities*
- IASB Exposure Draft *Leases*
- IASB presentation on *Different Measures for Measuring Uncertain Future Cash Flows*
- IASB Exposure Draft *Hedge Accounting*
- EFRAG Proactive project *Business Combinations under Common Control*
- IASB Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets*
- IASB project *Post-employment Benefits*
- IASB Exposure Draft *Insurance Contracts*
- IASB Exposure Draft *Revenue from Contracts with Customers*.

Highlights

Comment letters to the IASB

EFRAG finalised its comment letter to the IASB in response to the Request for Views on *Effective Dates and Transition Methods* (page 2).

EFRAG invited comments on its draft comment letters to the IASB on the IASB Exposure Draft *Offsetting Financial Assets and Financial Liabilities*. The draft comment letter welcomes the IASB and the FASB efforts to develop joint proposals for converged requirements for offsetting financial assets and liabilities. EFRAG supports the IASB decision to use, as a basis for the converged requirements, the existing guidance for offsetting financial assets and financial liabilities in IAS 32 *Financial Instruments: Presentation*, with some refinements. The comment deadline is 18 April 2011 (page 3).

IASB Request for Views on *Effective Dates and Transition Methods*

During its meeting, held by public conference call on 28 January 2011, EFRAG finalised its comment letter to the IASB in response to the Request for Views on *Effective Dates and Transition Methods* (the Request for Views). In view of the planned completion of a number of major projects in 2011, including *Financial Instruments, Leases, Revenue from Contracts with Customers* and *Insurance Contracts*, the IASB sought views of constituents on whether and how to sequence effective dates in order to reduce the burden on interested parties.

The comment letter suggests distinguishing between two groups of standards as follows:

- Group 1 – single effective date of 1 January 2015 at the earliest. This group include the standards resulting from the projects on *Revenue from Contracts with Customers, Leases, Insurance Contracts, Financial Instruments (IFRS 9)* and *Fair Value Measurement*.
- Group 2 – effective dates could be considered on a case-by-case basis and early adoption should be permitted. This group includes the standards resulting from the projects on *Post-employment benefits: Defined Benefit Plans* and *Presentation of Items of Other Comprehensive Income*. This group also includes the final standards on *Consolidation, Disclosure of Interests in Other Entities* and *Joint Arrangements*. EFRAG recommends that the latter three standards should be implemented at the same time.

The comment letter also suggests that different effective dates and earlier adoption could be permitted for first-time adopters for purely pragmatic reasons.

EFRAG Outreach Activities on *Financial Statement Presentation*

During its meeting, held by public conference call on 28 January 2011, EFRAG finalised its feedback report summarising views expressed by European constituents during the outreach meetings on the Financial Statement Presentation project, jointly organised with European National Standard Setters from September to December 2010.

The feedback report has been provided to the IASB and is available on EFRAG's website.

IASB supplementary document to Exposure Draft *Financial Instruments: Impairment*

On 31 January 2011, the IASB published, as a supplement to its November 2009 Exposure Draft *Financial Instruments: Amortised Cost and Impairment* (the ED), proposals for accounting for impairment of financial assets, such as loans managed in an open portfolio. This supplementary document is issued as a joint proposal with the FASB, to ensure common impairment solutions and to address concerns about operational difficulties of some proposals in the ED.

EFRAG discussed the proposals and welcomed overall the IASB's efforts to find operational solutions for the difficulties identified in respect of the model proposed in the ED. The draft comment letter will be finalised at the conference call scheduled for 24 February 2011.

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

In December 2010, the IASB published Amendments to IFRS 1: *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (the Amendments). The objectives of the Amendments are:

- to introduce an exemption for an entity that has been subject to severe hyperinflation to measure assets and liabilities at fair value and use that fair value as the deemed cost of those assets and liabilities in the opening IFRS statement of financial position; and
- to change certain references to fixed dates in IFRS 1 to refer to the date of transition to IFRSs.

EFRAG completed its initial assessment of the Amendments against the EU endorsement criteria and completed an initial study of its costs 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 are likely to exceed the costs of implementation. The date for launching the consultation on the draft endorsement advice and a draft effects study report is still to be determined.

IASB Exposure Draft *Offsetting Financial Assets and Financial Liabilities*

EFRAG finalised its draft comment letter to the IASB in response to the Exposure Draft *Offsetting Financial Assets and Financial Liabilities* (the ED). The draft comment letter welcomes the IASB and the FASB efforts to develop joint proposals for converged requirements for offsetting financial assets and liabilities. EFRAG supports the IASB decision to use, as a basis for the converged requirements, the existing guidance for offsetting financial assets and financial liabilities in IAS 32 *Financial instruments: Presentation*, with some refinements.

The draft comment letter supports the proposal to clarify that the right to set off the financial asset and the financial liability must be unconditional and legally enforceable in all circumstances. These criteria are currently applied under the existing IAS 32. The draft comment letter also supports the proposal to specify the disclosure requirements about rights to offset financial assets and financial liabilities of an entity and the related arrangements, including information about collateral and master netting arrangements. However, it urges the IASB to consider the proposals in the ED in the context of the existing disclosure requirements in IFRS 7 *Financial Instruments: Disclosures*, taking into account the disclosure proposals made in other consultation documents in respect of accounting for financial instruments. This is needed to ensure that the level of guidance included in the disclosure standard remains consistent and balanced across topics.

The draft comment letter is available on EFRAG's website. The comment deadline is 18 April 2011.

IASB Exposure Draft *Leases*

On 15 December 2010, EFRAG issued its comment letter to the IASB in response to the Exposure Draft *Leases* (the ED). In its comment letter, EFRAG raised a number of concerns about the proposals, including the concern that the boundary between leases (particularly those currently categorised as operating leases) and service contracts is difficult to determine. EFRAG noted that it was not convinced that the proposed criteria carried over from IFRIC 4 *Determining whether an Arrangement Contains a Lease* provide the necessary

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robust and operational distinction required to determine which (very different) accounting treatment is appropriate and most meaningful for the specific transaction.

At its February 2011 meeting, EFRAG discussed possible supplementary recommendations that it could make to the IASB to support their ongoing efforts in responding to EFRAG and other commentators' concerns. The discussion at the meeting was not conclusive.

EFRAG will continue the discussion at its next meeting.

IASB presentation on *Different Measures for Measuring Uncertain Future Cash Flows*

In several projects, the IASB proposed to require entities to measure assets and liabilities by reference to estimates of future cash flows. In some cases, when future cash flows are uncertain, the IASB proposed to use the expected value technique for measurement purposes. In responding to various IASB proposals, EFRAG has repeatedly objected to the use of the expected value technique in measuring individual or small populations of items, especially in the case of low-probability, high-impact scenarios or when evidence of the distribution of outcomes is unavailable. As this concern relates to the major projects, which the IASB intends to finalise this year, EFRAG invited an IASB delegation to explain why and how this measurement technique would provide more useful information to users of financial statements. The IASB staff made a presentation to EFRAG comparing different techniques for measuring assets and liabilities with uncertain future cash flows, including the expected value technique, the maximum amount that is more likely than not to occur and the most likely outcome. This topic will be considered by the IASB at its next meeting as a cross-cutting issue. EFRAG shared with the IASB staff its views on the different techniques for measuring assets and liabilities with uncertain cash flows, as previously expressed in comment letters on various IASB proposals. EFRAG did not take any decisions on the issue at its February 2011 meeting.

IASB Exposure Draft *Hedge Accounting*

In January 2011, EFRAG issued its draft comment letter to the IASB in response to the Exposure Draft *Hedge Accounting* (the ED). One of the concerns in the draft comment letter related to the non-eligibility for hedge accounting of a benchmark component in hedging a debt instrument with a negative indexation to the benchmark (the sub-LIBOR issue), which might create an inconsistency with risk management practices.

During its February 2011 meeting, EFRAG discussed different scenarios of sub-LIBOR exposures, focusing on the impact of hedge accounting on the combined net exposure. In addition, EFRAG considered an example of a risk management approach, which is applied by some financial institutions, but that was not considered by the IASB in developing the proposals in the ED. It was tentatively agreed to bring this matter to the IASB's attention.

The draft comment letter is available on EFRAG's website. The comment deadline is 2 March 2011.

EFRAG Proactive project *Business Combinations under Common Control*

At the December 2010 meeting, EFRAG discussed a model for the Business Combinations under Common Control project, whereby the requirements of existing IFRSs should apply before determining how the Framework and the reporting entity concept could assist in developing an approach to business combinations under common control. EFRAG generally supported the new approach, but directed staff to develop further some aspects of the model, particularly the indicators that are to be used to decide whether a business combination under common control has substance that is similar to a business combination with an unrelated party.

At its February 2011 meeting, EFRAG reviewed the refined proposals in respect of the indicators. Under the revised proposals, if the price of the transaction is not equal or similar to a market participant's price, then the transaction may not be accounted for under IFRS 3 *Business Combinations*, even if the transaction meets the definition of a business combination under IFRS 3. EFRAG agreed that, in those situations, IFRS 3 could not be applied as is. EFRAG recommended that a more detailed analysis be carried out to determine if and how IFRS 3 should be amended to address the specific difficulties arising from transactions under common control.

EFRAG also discussed the implications of business combinations under common control for the separate financial statements. EFRAG recommended that further analysis be carried out on whether there is anything specific to separate financial statements that would require accounting for a business combination under common control in the separate financial statements of the acquirer, different to the consolidated financial statements.

A refined paper, reflecting EFRAG's discussion, will be presented in a subsequent meeting.

IASB Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets*

In December 2010, the IASB published Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets* (the Amendments). The Amendments introduce an exception to the measurement principles in IAS 12 *Income Taxes* to provide a practical approach in those cases where it is difficult or subjective to determine the manner in which an entity expects to recover the carrying amount of its assets.

EFRAG discussed its initial assessment of the Amendments against the EU endorsement criteria and the initial study of its cost and benefits. The draft endorsement advice on the Amendments is subject to further discussions by EFRAG.

IASB project *Post-employment Benefits*

EFRAG discussed the developments resulting from the IASB's redeliberations of the proposals in the Exposure Draft *Defined Benefit Plans (Proposed amendments to IAS 19)* (the ED). The comment letter period on the ED ended on 6 September 2010 and the IASB is in the process of analysing the comments received.

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The ED proposed to split the pension cost into three components: service cost, finance cost and remeasurements, and to recognise the remeasurement component in other comprehensive income. During its redeliberations of the proposals in the ED, the IASB tentatively decided to allow an option of recognising the remeasurement component in profit or loss, provided that this election is irrevocable and could be done on a plan-by-plan basis.

EFRAG did not make any decisions at its February meeting. EFRAG will monitor the IASB's redeliberations on this project and will consider those at its next meetings.

IASB Exposure Draft *Insurance Contracts*

Although the comment period on the IASB Exposure Draft *Insurance Contracts* (the ED) closed on 30 November 2010, the insurance industry is still trying to find a compromise for one of the major concerns about the proposals in the ED – risk of artificial volatility in the statement of comprehensive income.

During its February 2011 meeting, EFRAG received an update from the HUB global insurance group (which represents a group of European, American, Japanese and Canadian insurance companies and trade bodies) on their proposed alternative to the proposals in the ED. The alternative proposals included a “top-down” approach for the discount rate for measuring insurance liabilities, allowing changes as a result of short-term movements in the discount rate being recognised in other comprehensive income, and not requiring discounting for property and casualty insurance if that would lead to the change in the insurer's business model. The objective of the update was educational, and EFRAG did not form any opinion on the alternative proposals.

EFRAG also continued discussing its alternative approach to the presentation in the statement of comprehensive income, focusing on the issue of whether a single format of presentation should be adopted across all industries to increase comparability between entities, or whether a different format should be developed for the insurance industry to provide more relevant information to the users of insurers' financial statements. EFRAG did not reach a tentative view and directed the staff to further develop two alternative models for presentation in the statement of comprehensive income. Both alternatives would be developed in expanded and in condensed formats. Once finalised, the alternative proposals would be shared with the IASB.

IASB Exposure Draft *Revenue from Contract with Customers*

In addition to its comment letter on the Exposure Draft *Revenue from Contracts with Customers* (the ED), EFRAG tentatively decided to provide input to the IASB's redeliberations process at the joint EFRAG-IASB meetings. At its February 2011 meeting, EFRAG continued discussing the developments resulting from the IASB's redeliberations of the proposals in the ED. It was noted that the IASB has recently made some tentative decisions that could lead to fewer changes to current practice than the original proposals in the ED. At this stage of the redeliberations process, it was not sufficiently clear what this would mean for the final standard. Therefore, EFRAG decided that it would be impracticable to provide valuable input to the IASB in February 2011.