

June 2014

Summary of EFRAG Technical Expert Group (TEG) meetings

EFRAG Consultative Forum of Standard Setters (EFRAG CFSS) held its quarterly meeting on 27 May 2014. The meeting primarily focused on the preparation of the ASAF meeting on 2 and 3 June and the following topics were discussed:

- IASB Project *Business Combinations under Common Control*
- IASB Project *Disclosure Initiative (Proposed amendments to IAS 1)*
- IASB Project *Accounting for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging*
- Bulletins on the IASB's *Conceptual Framework* Project and IASB Project *A Review of the Conceptual Framework for Financial Reporting*
- IASB Research Project *Equity Method of Accounting*

EFRAG TEG held conference calls on 28 May and 4 June 2014 to discuss:

- IASB Project *Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11)*
- IASB Project *Insurance Contracts*
- IASB Project *Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38)*
- EFRAG Short Discussion Series Paper IFRS 3 *Business Combinations – Subsequent Accounting for Acquisition Step-Ups*
- ESMA Consultation Paper *Guidelines on Alternative Performance Measures*

From 11-13 June 2014 EFRAG TEG held its monthly meeting. The following topics were discussed:

- IASB Project *Leases*
- EFRAG Discussion Paper *Classification of Claims*
- IASB Project *Equity Method in Separate Financial Statements*
- IASB Project *Accounting for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging*
- IASB Project *Revenue from Contracts with Customers*
- EFRAG/OIC/ICAC/DASB Discussion Paper *Separate Financial Statements*
- IASB Project *Insurance Contracts*
- IFRS Interpretations Committee Issues – IFRS 11 *Joint Arrangements*
- Bulletins on the IASB's *Conceptual Framework* Project and IASB Project *A Review of the Conceptual Framework for Financial Reporting*
- EFRAG Project *IAS 37 and IFRIC 21*
- IASB Project *Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11)*
- IASB Project *Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38)*
- EFRAG Project *Financial Statement Presentation*
- EFRAG/ASBJ/OIC/ICAI Joint Issues Paper *Goodwill: Reintroducing the Impairment and Amortisation Approach?*
- IFRS 3 *Business Combinations – Post-implementation Review*

Highlights

Endorsement Advices

EFRAG published an invitation to comment relating to the endorsement for use in the European Union and European Economic Area of the IASB Project *Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11)* on 16 June 2014. For more details please see page 3.

EFRAG published an invitation to comment relating to the endorsement for use in the European Union and European Economic Area of the IASB Project *Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38)* on 17 June 2014. For more details please see page 4.

Feedback Statements

EFRAG published on 13 June 2014 its feedback statement on a joint user outreach event held in Brussels relating to IFRS 3 *Business Combinations – Post-implementation Review*. For more details please see page 7.

IASB Project *Business Combinations under Common Control*

EFRAG CFSS members discussed the possible scope of the IASB project on Business Combinations under Common Control. It was noted that it would be beneficial if the IASB liaised with EFRAG and the OIC given their experiences with the joint Discussion Paper *Business Combinations under Common Control* and subsequent work and analyses performed since the publication of the feedback statement reflecting comments received. EFRAG CFSS members recommended the IASB to commence the project with a narrow scope by only looking at the consolidated financial statements. Furthermore, the EFRAG CFSS members recommended that the project should more particularly focus on transactions within the group where third parties were involved. Finally, it was recommended to analyse types of transactions where control was transitory (i.e. spin off followed by an initial public offering).

IASB Project *Disclosure Initiative (Proposed amendments to IAS 1)*

EFRAG CFSS members received an update on the proposed scope of the project and on the sub-topics that could be addressed. EFRAG CFSS members requested additional clarity on the scope of the project, the expected outcomes (e.g. discussion paper, exposure draft) and the expected publication work plan.

Furthermore, the EFRAG CFSS members recommended that the IASB leverage on the outcome of the 2011 Agenda Consultation and on the work that had already been done in the project on financial statements presentation that was stopped in 2010. They would expect as well leverage on the work done by EFRAG, the ANC and FRC on the Disclosure Framework.

Bulletins on the IASB's *Conceptual Framework Project* and IASB Project *A Review of the Conceptual Framework for Financial Reporting*

EFRAG CFSS members discussed papers prepared for the ASAF meeting on: the reporting of income and expense and the choice of measurement bases; executory contracts; and the business model. Members expressed different views on the papers.

EFRAG CFSS members also discussed the benefits of issuing Bulletins on the unit of account and cash flow statements. Given the IASB's timetable for finalising the exposure draft on the review of the Conceptual Framework, the view was expressed that it would not be possible to finalise the Bulletins in time to affect this work. However, the issues were considered important, and more work should be done although the outcome would be used for other purposes, for example, when commenting on the IASB's exposure draft on the review of the Conceptual Framework.

EFRAG CFSS members also expressed support for the paper discussing a conceptual approach to measurement and the use of other comprehensive income based on the business model and the concept of prudence that was considered as part of the next ASAF meeting papers.

At its June 2014 meeting, EFRAG TEG discussed the feedback received in response to the Bulletin on complexity. It was decided to prepare a feedback statement summarising the different views expressed on the issue. In addition, EFRAG TEG discussed the tentative decisions reached at the May IASB meeting. Concern was expressed in relation to how the IASB had tentatively decided to explain prudence. It was noted that without further explanation, the description did not seem to take into account that sometimes (but not always) it would provide more relevant information to have different recognition requirements for assets and liabilities (for example, it seemed relevant that the recognition requirements for assets and liabilities included in the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* were different).

IASB Research Project Equity Method of Accounting

EFRAG CFSS members discussed the IASB Research Project. EFRAG CFSS members were generally supportive of the identified areas for research, would such a Research project be needed. They however reiterated that, as had been identified during the IASB agenda consultation, a wholesale revision of the equity method was not a priority for Europe as there was no evidence that users were unhappy with the information provided. Greater clarity on how to use it was more important than a fundamental revision. They would therefore support efforts in the maintenance of the existing requirements, to ensure consistency in application.

IASB Project Accounting for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging

At the EFRAG CFSS meeting, EFRAG staff presented the main proposals in the IASB Discussion Paper and the very preliminary views held in EFRAG.

The project was further discussed at the June EFRAG TEG meeting with the objective of finalising a draft comment letter.

EFRAG TEG members confirmed that the outcome of the project should be a macro-hedge accounting model, and that the objective of representing risk management should not be pursued. They therefore dismissed the Portfolio Revaluation Approach applied to all managed portfolios. They expressed very positive appreciation of the IASB's analysis of bank current interest rate risk management practices and agreed to explore variants of the IASB Portfolio Revaluation Approach limited to mitigated risk. The variants would have to be tested for both reliability and feasibility and aim at improving the operability of the approach when limited to mitigated risk. They also agreed to seek views from constituents on a cash flow hedging model in the context envisaged by the Board, i.e. one that removes constraints of the current IAS 39 macro-hedge accounting model.

IASB Project Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11)

The project was discussed at both the May EFRAG TEG conference call and the June EFRAG TEG meeting.

EFRAG's initial assessment is that the Amendments satisfy the technical criteria for EU endorsement and EFRAG should therefore recommend their endorsement. Comments are requested by 16 July 2014. At the June EFRAG TEG meeting, the invitation to comment on the draft positive endorsement advice was approved.

IASB Project *Insurance Contracts*

The project was discussed at both the May EFRAG TEG conference call and the June EFRAG TEG meeting.

At its May 2014 conference call, and in advance of the ASAF meeting on 2 and 3 June, EFRAG TEG continued the discussions on the insurance industry alternative approach for participating contracts.

EFRAG TEG supported the alternative industry approach of using a current discount rate that reflected the characteristics of the liability in the balance sheet and a book yield discount rate for the recognition of the income statement interest expense. Any difference between the interest expense recognised using the book yield and the change in balance sheet liability using the current rate would be recognised either in the income statement or other comprehensive income depending on the entity's accounting policy choice.

EFRAG TEG confirmed its conclusion reflected in the comment letter that the contractual service margin should reflect the total unearned profit on the insurance contract. EFRAG TEG members reiterated their view that services (including asset management services remunerated by a share in the returns) that could not be distinctly unbundled from the insurance contract at inception should be considered as part of the services to be provided for the insurance contract as a whole and as a result should be considered as part of the contractual service margin.

EFRAG TEG supported the principle that the contractual service margin should be released in a pattern that best reflected the provision of the services under the insurance contracts. Specific guidance on how to release the contractual service margin for participating contracts would not be helpful.

EFRAG TEG supported the view that changes in the intrinsic value of options and guarantees should also be reflected in the contractual service margin. Changes in the time value of money of options and guarantees would be recognised either in the income statement or in other comprehensive income, depending on the entity's accounting policy choice. However, EFRAG TEG also supported that a practical expedient to allow the recognition of the entire changes in options and guarantees in the contractual service margin be considered, if it was impracticable for an entity to split changes in the cash flows from changes in the time value of options and guarantees.

At its June 2014 meeting, EFRAG TEG members received an update on the non-targeted issues re-deliberated by IASB in May 2014. The issues were recognising the contractual service margin in profit or loss, fixed-fee service contracts, significant insurance risk, portfolio transfers and business combinations. The update reflected the proposals in the IASB's 2013 ED, EFRAG's views on those proposals and the IASB's tentative decisions.

IASB Project *Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38)*

The project was discussed at both the May EFRAG TEG conference call and the June EFRAG TEG meeting.

At the conference call held on 4 June 2014, EFRAG TEG approved an invitation to comment relating to the endorsement of the project for use in the European Union and European Economic Area.

EFRAG's initial assessment is that the Amendments satisfy the technical criteria for endorsement and EFRAG should therefore recommend their endorsement. Comments are requested by 17 July 2014.

EFRAG Short Discussion Series Paper IFRS 3 *Business Combinations - Subsequent Accounting for Acquisition Step-Ups*

EFRAG TEG discussed a revised draft of a paper to discuss ways to provide information on the reversal of step-ups on assets acquired in a business combination, so as to address the perceived loss of relevance of the statement of income after a significant business combination.

EFRAG TEG exchanged views and required the staff to revise the paper to clarify constraints and implications of each alternative presented. The revised paper will be presented at a future meeting.

ESMA Consultation Paper *Guidelines on Alternative Performance Measures*

EFRAG TEG considered providing a feedback statement on the comments received from its constituents. However, as constituents provided broad support for EFRAG's original position in the draft comment letter, EFRAG TEG decided that it was not necessary to publish a feedback statement.

IASB Project *Leases*

Representatives of Lease Europe gave a presentation to illustrate the leasing industry's views on the project. EFRAG TEG approved, in principle, the launch of an additional public consultation in cooperation with the ANC, DRSC, OIC and FRC to seek further input from European constituents after the IASB's decision of not modifying the definition of a lease as exposed in the 2013 ED. The input relates to type of transactions that should not be recognised as leases and constituents' views on the diverging approaches to lessee accounting that the IASB and the FASB have tentatively supported at the March 2014 meeting as well as evidence of comparative costs associated with the implementation of the two models.

EFRAG Discussion Paper *Classification of Claims*

EFRAG TEG approved for publication a paper on classification requirements for the claims on an entity. The IASB plans to release a Discussion Paper on the equity/liability distinction at approximately the same time as the publication of an Exposure Draft of the entire revised Conceptual Framework. Therefore, the EFRAG discussion paper has been written to contribute to the IASB's Discussion Paper and assist constituents in engaging with the project.

The Paper does not aim at defining how to distinguish between claims. Rather, the Paper discusses the objectives of classification requirements and approaches to defining elements, as well as aiming to identify the choices that must be made in classifying the claims on an entity and the consequences of those choices. The paper also identifies the extent to which each of the choices is consistent with the identified objectives and how these objectives may conflict with each other.

IASB Project *Equity Method in Separate Financial Statements*

EFRAG TEG was provided with the latest developments regarding the IASB's project. EFRAG TEG was also provided with the feedback received on the expected implementation consequences of the application of the equity method in separate financial statements in European jurisdictions that allow or require entities to prepare annual accounts in conformity with IFRS. It was noted that none of the respondents expected significant extra costs and that a number of the respondents had identified some benefits derived from the application of the equity method in separate financial statements. No decisions were taken at the meeting.

IASB Project Revenue from Contracts with Customers

The IASB published its new standard on revenue recognition on 28 May 2014. EFRAG TEG addressed some issues related to the future endorsement advice that might be requested on IFRS 15 *Revenue from Contracts with Customers*, including what sort of analysis EFRAG TEG should prepare in its future new role as advisor to its Board. No decisions were taken.

EFRAG/OIC/ICAC/DASB Discussion Paper Separate Financial Statements

EFRAG TEG discussed a draft Discussion Paper on Separate Financial Statements. The Discussion Paper sets out the framework of separate financial statements in Europe, provides the key conclusions from the research activities on the information needs of users and analyses a number of financial reporting areas identified by those applying and using separate financial statements. A revised draft will be considered at a future meeting for final approval.

IFRS Interpretations Committee Issues - IFRS 11 Joint Arrangements

EFRAG TEG considered an EFRAG staff paper summarising the IFRS Interpretation Committee's decisions and recent developments in relation to IFRS 11 *Joint Arrangements*. EFRAG TEG also discussed a finalised IFRS Interpretation Committee's Agenda Decision concerning whether the assessment of 'other facts and circumstances' should be undertaken with a view only towards whether those facts and circumstances create enforceable rights to the assets and obligations for the liabilities or whether that assessment should also consider the design and purpose of the joint arrangement, the entity's business needs and the entity's past practices.

Some EFRAG TEG members expressed their support for the IFRS Interpretation Committee's final Agenda Decision. EFRAG TEG asked the EFRAG staff to provide practical examples that would facilitate the discussion on IFRS 11 implementation issues at a future meeting.

EFRAG Project IAS 37 and IFRIC 21

EFRAG staff presented a draft of a discussion paper that explored different ways to address concerns raised by constituents during the endorsement process of IFRIC 21 *Levies*. The paper considered, among others, possible changes to the definition of a liability.

EFRAG TEG exchanged views on the different alternatives presented in the paper. One of the challenges is to identify the period to which the levy relates to and whether the payment of the levy gives rise to an asset. EFRAG staff will consider the comments and bring back the paper at a future meeting.

EFRAG Project Financial Statement Presentation

EFRAG staff presented a revised version of a short discussion series paper, in which it explored how the IASB could leverage on the work previously performed in the Financial Statement Presentation project to assist in its standard setting effort to bring improvements to presentation and disclosure in financial reporting.

While confirming that improvements to presentation and disclosure in financial reporting is a priority, EFRAG TEG recommended to not pursue this paper as a support to public consultation, noting that constituents are already being asked to react to many IASB and EFRAG papers and there is a risk of consultation fatigue.

EFRAG/ASBJ/OIC/ICAI Joint Issues Paper *Goodwill: Reintroducing the Impairment and Amortisation Approach?*

EFRAG staff presented a revised version of a staff paper jointly developed by EFRAG's Research team, the OIC, and the Accounting Standards Board of Japan (ASBJ), and supported also by the Institute of Chartered Accountants of India (ICAI). This paper discusses alternatives for the subsequent accounting of goodwill, including the reintroduction of an amortisation and impairment approach.

Mr. Yukio Ono, chairman of the ASBJ, and ASBJ Board member Tomo Sekiguchi attended via videoconference.

EFRAG TEG approved that the paper would be issued as a joint Staff paper and delegated the Research team to best accommodate comments made in the meeting

IFRS 3 *Business Combinations* - Post-implementation Review

EFRAG TEG discussed the feedback received in a number of outreaches conducted with users and preparers on the experience with, and the effect of, implementing IFRS 3 *Business Combinations*. The outreach activities took place between March and June 2014 and comprised a series of discussions with European users and preparers in the form of events, meetings, interviews and completion of questionnaires. The outreaches were organised together with some National Standard Setters and European user organisations, notably the European Federation of Financial Analysts Societies (EFFAS). The outreach activities included an event held in Brussels on 1 April with investors, analysts and a range of other stakeholders; and a number of interviews that involved several investors and analysts. A feedback statement on the 1 April event has been published. The feedback statement on the views gathered through interviews with investors and analysts, is expected to be published soon.

EFRAG TEG also discussed EFRAG's letter to the IASB in response to the Request for Information, which highlighted the major concerns identified by the users and preparers. EFRAG TEG approved the letter to the IASB on the Request for Information, subject to drafting. EFRAG's letter will be supported by the feedback reports on the outreach activities on IFRS 3. The feedback evidences that there are areas of the Standards, such as the requirement to have separate recognition of intangible assets from goodwill that can be challenging and costly to implement for preparers. It also demonstrates, that in several cases, the usefulness of the information provided by financial statements is being questioned by users, who request different or additional information about a business combination and its effects.