

IFRS in Brief

December 2009, **Issue 64**

This issue of IFRS in Brief covers the December 2009 meeting of the International Accounting Standards Board (IASB or Board); a number of the sessions involved joint discussion with the U.S. Financial Accounting Standards Board (FASB) (together, the Boards).

Highlights

- Converged fair value measurement requirements expected by September 2010
- Limited scope re-exposure of liabilities project expected in December 2009 with a 12 April 2010 comment deadline and a working draft of the new liability standard expected in February 2010
- Discontinued operations guidance expected to be re-exposed
- Major projects completed in 2010 and 2011 are expected to have effective periods no earlier than 1 January 2012 and 1 January 2013 respectively.

**KPMG's monthly update on
International Financial Reporting
Standards (IFRSs)**

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Summary

At its December 2009 meeting, the IASB continued discussing the:

- Board's response to the financial crisis
- joint ventures project
- liabilities project
- discontinued operations project
- emissions trading schemes project
- insurance contracts project
- financial statement presentation project
- revenue recognition project
- leases project
- conceptual framework project
- post-employment benefits project

The Board also discussed certain aspects relating to the effective dates of new requirements.

The Board's Response to the Financial Crisis

The Board discussed the following projects that relate to the financial crisis:

- consolidation
- fair value measurement
- hedging
- classification and measurement: financial liabilities
- derecognition
- financial instruments with characteristics of equity.

Consolidation

The Boards held a joint education session to discuss the definition

of control, control with less than a majority of the voting rights and agency relationships; no decisions were made on this topic.

Fair Value Measurement

The Boards agreed to work towards eliminating differences between the IASB's exposure draft (ED) on fair value measurement and the FASB *Accounting Standards Codification Topic 820 (Fair Value Measurements and Disclosures)*.

The Boards plan to have converged fair value measurement requirements by September 2010.

Hedging

The Boards discussed the feedback received from their recent outreach activities. They discussed also the relationship between risk management and financial reporting in relation to the reporting of hedging activities; no decisions were made on this topic.

Classification and Measurement: Financial Liabilities

The Board discussed feedback received during recent outreach activities related to possible approaches for consideration of "own credit risk" in the remeasurement of financial liabilities; no decisions were made on this topic.

Derecognition

The Board discussed comments received, in response to the Derecognition ED, for financial liabilities and decided tentatively that:

- a financial liability is extinguished and would be derecognised when the contract is substantially modified
 - a financial liability contract that is altered would be considered substantially modified when:
 - changes in the timing, amounts or uncertainty of the cash flows of the new / modified contract
- are substantially different from the original contract; or
- the alteration changes the nature of the debtor's obligation or the nature of the investment that the contract represents
- the extinguishment of a financial liability would be accounted for using the current guidance in IAS 39 *Financial Instruments: Recognition and Measurement* all transaction costs and fees incurred related to the extinguishment of the original liability would be included in the gain or loss recognised on extinguishment unless they are directly attributable to a new liability
 - in accounting for a modification of a financial liability that does not meet the criteria for extinguishment accounting, an entity would follow the current guidance in IAS 39
 - a partial extinguishment of a financial liability effected by repurchasing part of the liability would be accounted for in accordance with IAS 39; whether there is a substantial modification would be assessed on a contract-by-contract basis; the substantial modification guidance would not be applied to part of a financial liability
 - the guidance in IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* would be incorporated into the derecognition ED for the extinguishment of an entire financial liability; the ED would clarify that the difference, if any, between the fair value of the liability extinguished and the fair value of the equity instruments issued as consideration would, to the extent it qualifies as an asset or liability, adjust the gain or loss to be recognised on derecognition
 - if the substantial modification criteria are met, the derecognition accounting by the borrower and lender would be symmetrical.

Financial Instruments with Characteristics of Equity

The Boards continued discussing a classification approach for financial instruments with characteristics of equity and decided tentatively:

- to retain, notwithstanding the decisions reached in this project, the existing reporting requirements for instruments currently accounted for in accordance with IFRS 2 *Share-based Payment* and FASB *Accounting Standards Codification™ Topic 718, Stock Compensation*
- to report on the statement of financial position as offsetting debit and credit instruments any physically settled forward purchase contracts; the credit instrument would be a liability, measured at the total future payment discounted to its present value using an appropriate market interest rate for an equivalent cash-settled instrument; the debit would be reported as an offset to equity, but no decision was made as to whether the offset would be considered a reduction in the number of outstanding shares.

The Boards will continue to consider principles or exceptions for determining which types of share-settled instruments would be classified as equity.

Joint Ventures

The Board discussed the inconsistencies in the accounting for gains and losses on the contribution of non-monetary assets to jointly controlled entities under SIC-13 *Jointly Controlled Entities – Non-Monetary Contributions by Ventures* and IAS 27 *Consolidated and Separate Financial Statements*. The Board decided tentatively that:

- the inconsistencies would be dealt with separately from the joint ventures project
- the SIC-13 requirements and any guidance relating to accounting

for joint ventures using the equity method would be incorporated as consequential amendments to IAS 28 *Investments in Associates*.

The Board also discussed comments received on the ED regarding the accounting for transactions between the parties and their joint arrangements and decided tentatively:

- that the SIC-13 guidance requiring gains and losses to be measured reliably for recognition on the contribution of non-monetary assets would not be included in the amendment as this guidance is already included in the *Framework*
- to allow recognition of gains or losses resulting from the contribution of non-monetary assets only if the transaction has commercial substance
- to carry forward the IAS 31 *Interests in Joint Ventures* requirement to fully recognise losses when the contribution, sale or purchase evidences a reduction in the net recoverable amount of the assets contributed, sold or purchased
- to clarify that when a joint operation is structured through an entity, transactions between the parties and the joint operation are in effect transaction between the parties themselves.

Liabilities

The Board reaffirmed its previous tentative decision to:

- expose for public comment only the proposals to clarify the measurement requirements of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* (see IFRS Briefing Sheet issue 152); the Board aims to publish a limited scope ED in December 2009 with a comment deadline of 12 April 2010
- post in February 2010 a working draft of the new standard on the IASB website.

Discontinued Operations

The Board reconsidered the following issues previously discussed at its July 2009 meeting:

- the recognition of impairment losses when the losses are greater than the carrying amount of the disposal group's non-current assets
- the presentation of other comprehensive income (OCI) relating to discontinued operations in the statement of comprehensive income
- the possible disclosure of accumulated other comprehensive income (AOCI) related to discontinued operations
- concerns raised by constituents relating to the reversal of impairment losses.

As a result of the discussions the Board decided:

- not to add a project addressing impairment measurement and reversals to its agenda
- that any AOCI and OCI disclosure amendments would be considered as part of the financial statement presentation project.

The IASB also discussed the following discontinued operations project issues jointly with the FASB:

- definition of discontinued operations
- disclosures about discontinued operations and other disposals
- effective date and transition date for the proposed guidance.

Definition of Discontinued Operations

The Boards decided tentatively that a discontinued operation is "a component that has either been disposed of, or is classified as held for sale, and

- represents a separate major line of business or geographical area of operations;

- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is a business that meets the criteria to be classified as held for sale on acquisition."

Disclosures About Discontinued Operations and Other Disposals

The Boards decided tentatively that an entity would disclose the following information for the current and prior periods:

- for a discontinued operation:
 - the profit or loss, including major income and expense items making up that profit or loss such as impairments, interest, depreciation and amortisation
 - the major classes of cash flows
 - the major classes of assets and liabilities classified as held for sale in the notes to the financial statements reconciled to total assets and total liabilities classified as held for sale as presented separately on the face of the statement of financial position
 - the profit or loss for disposals presented in the notes to the financial statements reconciled to the after-tax profit or loss from discontinued operations as presented in the statement of comprehensive income
 - the profit or loss attributable to the parent when the component includes a non-controlling interest
- disposal of a component that does not meet the definition of discontinued operations:
 - the pre-tax profit or loss
 - the major classes of assets and liabilities classified as held for sale in the notes to the financial statements reconciled to total assets, and total liabilities classified as held for sale that

- are presented separately in the statement of financial position
- the profit or loss for disposals presented in the notes to the financial statements reconciled to the after-tax profit or loss from discontinued operations presented in the statement of comprehensive income
- the profit or loss attributable to the parent when the component includes a non-controlling interest
- for disposals of long-lived assets that are not components of an entity:
 - if not present separately in the statement of financial position an entity would disclose major classes of assets and liabilities included as part of a disposal group on the notes the financial statements reconciled to total assets and total liabilities classified as held for sale that are presented separately in the statement of financial position
- when there is continuing involvement and continuing cash flows:
 - the nature of the activities that give rise to continuing involvement and / or cash flows
 - the period the continuing involvement and / or cash flows is expected to last
 - if applicable, the amount of the continuing cash flows
 - the amounts presented in continuing operations after the disposal transaction that prior to the disposal transaction would be consider intra-entity transactions and eliminated in consolidated financial statements.

Effective Date and Transition Date for the Proposed Guidance

The Boards decided to re-expose the guidance in the form of an ED; the length of the comment period will be discussed at a future meeting.

Emissions Trading Schemes

The IASB discussed two alternatives for the accounting for the right to receive future allowances in a cap and trade scheme. The discussion centred around when an entity controls a resource related to future instalments. The alternatives are:

- as the contingencies to holding the right are resolved; or
- when an entity holds the right to receive the allowances if it takes specified actions.

No decisions were made on this topic. The Boards plan to discuss emissions trading scheme accounting models further in the first quarter of 2010.

Insurance Contracts

The IASB considered whether insurance contract remeasurements could be presented in other comprehensive income when the liability is backed by assets not carried at fair value through profit or loss and decided tentatively that:

- the accounting for an insurer's assets would not change
- OCI recognition would not be permitted or required for such insurance contracts.

The IASB also discussed the insurance project jointly with the FASB, and the Boards decided tentatively that:

- the measurement approach for insurance liabilities would reflect the current assessment of the insurer's obligation using the following building blocks:
 - unbiased, probability-weighted average future cash flows expected to arise as the insurer fulfils the obligation, risk adjusted based on the insurer's view of the uncertainty in the timing and amount of the future cash flows

- the time value of money
- an amount that eliminates any gain at the contract's inception.
- an insurance liability would not be remeasured for changes in the risk of non-performance by the insurer.

The Boards noted the reasons why the insurance project is following a measurement approach for insurance liabilities based on future cash flows, as opposed to the approach under development in the revenue recognition project.

The Boards will continue their discussion of this project in January.

Financial Statement Presentation

The IASB and FASB discussed:

- definition and presentation of remeasurements
- application of the cohesiveness principle
- presentation on the statement of financial position
- presentation of the effects of basket transactions
- presentation of foreign currency transaction gains and losses.

Definition and Presentation of Remeasurements

The IASB confirmed their previous tentative position to require the presentation of remeasurements, including explanatory information in the notes to the financial statements arranged by section and category.

The FASB confirmed their previous tentative decision to require disaggregation of remeasurements in the statement of comprehensive income in columnar format.

Earlier in the week, the IASB decided tentatively that a remeasurement would be defined as "an amount recognised in comprehensive income that reflects the effects of a change in the carrying amount of an asset

or liability to a current price or value (or to an estimate of a current price or value). A current price or value includes the following measurement attributes: fair value, fair value less costs to sell, value in use and net realisable value.”

Application of the Cohesiveness Principle

The Boards decided tentatively:

- to require the application of the cohesiveness principle at the category level in the statement of financial position, the statement of comprehensive income and the statement of cash flows
- that items in the financial statements, generally would be classified by reference to how the related assets and liabilities are classified on the statement of financial position
- to add a “financing arising from operating activities” category to the business section in the statement of financial position and the statement of comprehensive income; the category would include long-term liabilities tied to operating activities, for example, a pensions liability; cash flows relating to this category would be classified under a new heading “financing arising from operating activities” in the statement of cash flows.

Presentation on the Statement of Financial Position

The Boards decided tentatively:

- that management is in the best position to decide whether to present a statement of financial position on a classified basis or order of liquidity basis
- that a classified statement of financial position would present assets and liabilities in short-term and long-term subcategories based on a fixed one-year period and these subcategories would be subtotalled

- to require presentation of total assets and total liabilities on the statement of financial position
- to remove the discussion paper (DP) proposal requiring an entity to disclose information about the maturities of short-term contractual assets and liabilities in the notes to financial statements
- to specify that an entity would classify its cash balance at the reporting entity level, rather than at the reportable segment level; cash will therefore be presented in one category on the statement of financial position
- to eliminate the concept of cash equivalents and require such assets to be presented as short-term investments in the statement of financial position
- to specify that an entity would present bank overdrafts in the debt category of the financing section of the statement of financial position
- that if assets and liabilities are of the same nature and are measured differently, the measurement basis should be used for further disaggregation on the statement of financial position.

In addition, the IASB voted to specify in their ED minimum line items for the statement of financial position from IAS 1 *Presentation of Financial Statements*, while the FASB voted not to specify such in their ED.

Presentation of the Effects of Basket Transactions

The Boards decided tentatively that an entity would present the effects of a basket transaction in a distinct section in the statement of comprehensive income and the statement of cash flows.

Presentation of Foreign Currency Transaction Gains and Losses

The Boards decided tentatively to require presentation of foreign currency transaction gains and losses in the same section / category as the assets

and liabilities that give rise to the gains or losses; the Boards noted that this would include the components of the net gain or loss on remeasuring the financial statements of an entity into its functional currency.

Revenue Recognition

The IASB and FASB discussed:

- warranties and product liability
- rights of return
- estimates of uncertain consideration.

Warranties and Product Liability

The Boards decided tentatively that:

- for a warranty for defects that exist at the time the asset is transferred to the customer, no separate performance obligation exists; rather it is treated as if the entity has not satisfied its performance obligation to transfer the asset; accordingly, at the end of the reporting period an entity would determine the likelihood and extent of defects in the assets it has sold to customers and:
 - for defective assets that the entity would have to replace, no revenue would be recognised
 - for defective assets that the entity would have to repair, revenue would not be recognised for the components of the product sold that the entity would have to replace when repairing the product
- for a warranty that provides a customer with cover for faults arising after the product is transferred to the customer, a separate performance obligation exists. Therefore, an entity would allocate part of the transaction price to a warranty liability
- if, by law, an entity is required to pay compensation should its products cause harm or damage then no separate performance obligation exists and the entity

would account for such obligations in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Rights of Return

When accounting for the sale of goods in which the purchaser has a right of return, the Boards decided tentatively that:

- an entity would not recognise revenue for goods that are expected to be returned, but rather a refund liability would be recognised for the expected amount of refunds to customers, measured on a probability-weighted basis
- the refund liability and the amount allocated to the performance obligations would be updated for changes in expectations of the amount of refunds
- an asset and corresponding adjustment to cost of sales would be recognised, at the original cost of the goods, for the right to recover goods from customers on settling the refund liability
- the promised return service would not be a separate performance obligation from the refund liability.

Estimates of Uncertain Consideration

The Boards decided tentatively that if an entity could identify possible outcomes and reasonably estimate the probabilities of these outcomes, then an estimate of the uncertain consideration would be included in the transaction price.

The ED is expected to include some guidance in this respect in the context of revenue recognition, the Boards decided tentatively that an entity can identify the possible outcomes of a contract and reasonably estimate the related probabilities only if the entity has experience with identical or similar types of contracts and does not expect circumstances surrounding those types of contracts to change significantly.

The Boards plan to consider disclosure and scope aspects of the revenue recognition project at their January joint meeting.

Leases

The Boards decided tentatively that:

- the obligation recognised by the lessee and the receivable recognised by the lessor, would include amounts payable under contingent rental arrangements, provided in the case of the lessor it could be measured reliably
- the obligation / receivable would be measured using an expected outcome technique and would be reassessed at each reporting date if any new facts or circumstances indicate that there is a material change in the obligation
- contingent rentals based on an index or rate would be measured using readily-available forward rates or the rates at the inception of the lease if forward rates are not readily available
- lessees would account for residual value guarantees in the same way as contingent rental arrangements
- the following would be excluded from the scope of the proposed new requirements:
 - leases of intangible assets and biological assets
 - leases to explore for or use natural resources, such as minerals, oil and natural gas
- it would not provide a scope exclusion for leases of non-core assets.

The Boards also instructed the staff to provide additional analysis on whether a scope exclusion would be provided for short-term leases.

The Boards plan to continue discussing lessee and lessor accounting issues at their January joint meeting.

Conceptual Framework: Phase C

The Boards discussed measurement concepts as well as credit risk in liability

measurement for potential inclusion in a DP. The Boards deferred the drafting of the DP pending further work on the staff paper.

Post-employment Benefits

At previous meetings, the Board decided tentatively that entities would disaggregate changes in the net defined benefit asset or liability into service cost, interest cost and remeasurement components. The remeasurement component would be recognised in the other comprehensive income section of the statement of comprehensive income. In December the Board further discussed the definition of the remeasurement component and decided tentatively that the remeasurement component:

- would include changes in the service costs estimate
- would exclude the interest income or expense on the net defined benefit asset or liability.

The Board is expected to consider the disclosure requirements proposed in the post-employment benefits project ED at their January 2010 meeting.

Effective Dates

In order to allow users of IFRS sufficient time to prepare for the adoption of new requirements the Board decided to work towards the following arrangements relating to effective dates:

- new requirements would be effective for annual periods beginning on or after a certain date as opposed to for periods ending on a certain date
- effective dates would be restricted to 1 January and 1 July
- major projects completed in 2010 and 2011 would have effective periods no earlier than 1 January 2012 and 1 January 2013 respectively.

The Board also decided to seek feedback on the way that transitional provisions are developed and written.

IASB Observer Notes

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