

# IFRS in Brief

November 2007, **Issue 40**

This issue of IFRS in Brief covers the October 2007 meeting of the International Accounting Standards Board (IASB) and the October 2007 joint meeting of the IASB and the U.S. Financial Accounting Standards Board (FASB).

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

**AUDIT ■ TAX ■ ADVISORY**

ED of *State-controlled Entities and the Definition of a Related Party*

- the financial instruments project.

In addition, at its October 2007 meeting the IASB:

- considered topics for its second annual improvements project
- discussed an amendment proposed by the IFRIC to IFRS 2 *Share-based Payment* and IFRIC 11 *IFRS 2 – Group and Treasury Share Transactions*
- received an update on eXtensible Business Reporting Language (XBRL).

At the October 2007 joint meeting of the IASB and the FASB, the Boards discussed the:

## Summary

At its October 2007 meeting the IASB continued discussing:

- the conceptual framework project
- the fair value measurement guidance project
- the forthcoming round-table discussions on the Exposure Draft (ED) of *Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation*
- the financial statement presentation project
- proposals in the ED of *Proposed Amendments to IAS 37 Provisions, Contingent Liabilities and Contingent Assets and IAS 19 Employee Benefits*
- the lease accounting project
- the post-employment benefits project
- amendments to IAS 24 *Related Party Disclosures* proposed in the

- conceptual framework project
- financial statement presentation project
- revenue recognition project
- derecognition of assets and liabilities.

## IASB Meeting

### Conceptual Framework

The Board discussed three main areas with respect to the conceptual framework:

- the interaction between the new and existing frameworks
- the objective of financial reporting
- the definition of an asset under Phase B *Elements and Recognition*.

With regard to the interaction between the new and existing frameworks the Board tentatively decided that:

- when Chapters 1 and 2 of the new framework are finalised they would replace the relevant paragraphs on the objective and qualitative characteristics of financial reporting in the existing *Framework*
- new chapters, other than Chapters 1 and 2, would not change the existing *Framework*, unless essential
- the new framework would not result in changes to IFRSs
- the effective date for application of each chapter would be at least one year from the date it is finalised in order to allow application of the guidance contained in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, whereby in the absence of an applicable IFRS, management are required to consider the *Framework*.

With regard to the objective of financial reporting the Board asked the staff to consider whether users of financial reports, other than capital providers, should be explicitly acknowledged in the proposed objective.

For the definition of an asset under Phase B *Elements and Recognition* the Board tentatively decided that the definition would:

- focus on a present economic resource as opposed to future inflows of economic benefits
- not include any reference to probability
- focus on the present.

It was noted that the FASB reached similar decisions at its October meeting (see below).

### Fair Value Measurements

The Board tentatively decided that the objective of the project would be “to develop principles and measurement

guidance for fair value measurements in IFRSs”

The Board confirmed that the fair value measurements currently required or permitted by all standards would be reviewed. As a result the Board plans to:

- assess whether an exit price was the measurement basis intended by each standard
- when an exit price was not the measurement basis intended, consider whether additional guidance should be developed.

The related ED was previously expected to be published in early 2008. The Board now expects this ED to be published in the second half of 2009.

### Financial Instruments Puttable at Fair Value

The Board confirmed with regard to the planned 12 November public round-table discussions on the ED of *Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation* that the following questions would be focused on:

- The proposed amendment is a product of a short-term project aimed at creating a limited exception to the classification requirements of IAS 32 *Financial Instruments: Presentation*. Within that context does the exception contained in the proposed amendment meet the project’s objectives? If not, why and what would you propose?
- Are the proposals operational? If not, why and what changes would you propose?
- Are there any issues not addressed in the staff draft that should be addressed? If so, what are they and why should they be addressed?

A staff draft of a proposed amendment will form the basis for the round-table discussions.

### Financial Statement Presentation

The Board discussed the statement of cash flows and tentatively decided that:

- offsetting of cash inflows and outflows relating to items currently classified as cash equivalents would be permitted
- the application guidance with respect to net cash flows reporting for financial institutions in paragraph 24(a) - (c) of IAS 7 *Statement of Cash Flows* would be retained.

The Board discussed foreign currency translation adjustments and tentatively decided that:

- for consolidated subsidiaries and joint ventures accounted for using the proportionate consolidation method, foreign currency translation adjustments should be presented in a new separate section of the statement of comprehensive income
- for equity method investments, the classification of foreign currency translation adjustments in the statement of comprehensive income should mirror the category in which they are classified for the statement of financial position.

The Board confirmed that in relation to capital management disclosures:

- only equity and financial liabilities that are managed as capital should be included
- items included in the operating category should not be included.

The Board also tentatively decided that:

- the classification of ordinary dividends payable and related changes in the financial statements would be based on such dividends being classified as a liability (therefore no equity treatment)
- the effects of a single transaction that involves multiple assets (or a combination of assets and liabilities)

that would be classified in more than one category of asset and / or liability (a basket transaction) should, in principle, be reflected in each of the relevant categories where the related assets and liabilities would be classified.

### Provisions

The Board continued redeliberating proposals in the ED of *Proposed Amendments to IAS 37 and IAS 19*. The Board discussed (with the assistance of examples) the uncertainty about the existence of a present obligation and the resulting impact on the recognition and measurement of liabilities. The Board tentatively decided that a liability should be recognised if the available evidence indicates that the reporting entity has an obligation.

The Board also tentatively decided not to provide guidance on a probability threshold (such as “more likely than not”) for determining if a liability exists because, in the Board’s view, determining if a liability exists is a matter of judgement based upon all available evidence.

### Leases

The Board discussed additional lessee obligations that arise as a result of entering into lease arrangements and also variable lease payments.

The Board tentatively decided that additional lessee obligations that arise as a result of entering into a lease arrangement are liabilities that exist at the commencement of the lease term.

The Board discussed, but did not conclude on, the following matters in relation to such obligations:

- measurement of the resulting liability
- the corresponding debit entry on recognition of the liability
- whether the obligation results in an asset of the lessor.

As a result of its discussion on variable lease rentals, the Board tentatively decided that for rentals that are linked to an index or market rentals, a liability exists for the lessee at the commencement of the lease term in respect of both the fixed and variable rental components. The Board discussed, but did not conclude on, the measurement of liabilities resulting from such variable lease rentals (if they exist).

### Post-employment Benefits

The Board discussed the definitions of benefit promises and tentatively decided that:

- the nature of the benefit promise should be considered in the accumulation phase only
- longevity risk should not have an impact on benefit promise classification.

The Board also observed that irrespective of the classification of the benefit promise, the measurement of the employer’s liability would include longevity risk.

The Board tentatively decided that in each of the accumulation, deferment and payout phases the benefit promise liability should be measured according to its classification.

### Related Party Disclosures

The Board recommenced discussing the proposed amendments to IAS 24 contained in the ED of *State-controlled Entities and the Definition of a Related Party* based on the comment letters received.

The Board clarified that the state-controlled disclosure exemption would not be available if either the reporting entity or the other state-controlled entity influenced:

- the transaction, or
- the operating and financial policies of the other entity.

The Board tentatively decided that:

- non-state-controlled entities would not be allowed to avail of the exemption
- a subsidiary (not state-controlled) whose parent prepares consolidated financial statements available for public use would not avail of the exemption
- the fundamental definition of a related party would not be revisited
- a “best endeavours” clause would not be included.

The Board also tentatively decided that materiality guidelines for related party transactions would not be included.

### Financial Instruments

The Board discussed certain cash flow hedge application issues for hedging portfolios of items with interest rate risk presented by the staff. In respect of the issues identified, the Board tentatively decided that changes to IAS 39 *Financial Instruments: Recognition and Measurement* should be considered by the staff.

### Annual Improvements

As part of its second annual improvements ED, expected to be published in October 2008, the Board considered two proposed improvements recommended by the IFRIC:

- IAS 18 *Revenue* – Determining whether an entity is acting as a principal or as an agent: The Board tentatively decided that high-level guidance on this issue should be included in the Appendix to IAS 18. The staff was instructed to prepare the required amendment.
- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* – Disclosures required for non-current assets (or disposal groups) classified as held for sale or discontinued operations: The Board recognised that disclosure requirements with

respect to assets or disposal groups within the scope of IFRS 5 are in need of clarification and decided to consider this topic at a future Board meeting yet to be determined.

### Share-based Payment

The IFRIC had previously been asked for guidance on accounting for group cash-settled share-based payment transactions in the financial statements of a subsidiary in situations when:

- it is the parent who has the obligation to make cash payments to the employees of the subsidiary
- the cash payments are linked to the price of the equity instruments of either the subsidiary or the subsidiary's parent.

The Board discussed and agreed with a proposal by the IFRIC to amend IFRS 2 *Share-based Payment* and IFRIC 11 *IFRS 2 – Group and Treasury Share Transactions* in relation to the situation outlined above to specify that in the financial statements of the subsidiary:

- IFRS 2 should be applied
- the measurement of the employee services should be in accordance with the requirements for cash-settled share-based payment transactions.

The staff was instructed to prepare an ED of the proposed amendments.

### XBRL

The International Accounting Standards Committee Foundation XBRL team provided an educational

update to the Board on global adoption of XBRL and how it links in with IASB projects. No decisions were made in respect of this topic.

### Joint meeting of the IASB and the FASB

#### Conceptual Framework

The Boards tentatively decided that:

- there would be a 120-day comment period in respect of the forthcoming ED on Phase A *Objective and Qualitative Characteristics of Financial Reporting*
- as part of Phase B *Elements and Recognition*, an asset of an entity would be "a present economic resource to which, through an enforceable right or other means, the entity has access or can limit the access of others"

#### Financial Statement Presentation

The Boards discussed the forthcoming discussion paper on financial statement presentation which is expected to be published in the second quarter of 2008. The Boards provided their preliminary views on the discussion paper and discussed its content and style. The Boards supported the overall structure of the discussion paper. No technical decisions were made in respect of this topic.

#### Revenue Recognition

The staff presented an educational session to the Boards on the *fair value* (assets and liabilities would be measured at fair value) and the *allocated customer consideration*

(assets and liabilities would be measured by reference to the customer consideration) revenue recognition models, which were developed as part of the joint revenue recognition project. No technical decisions were made.

#### Derecognition of Assets and Liabilities

The staff presented to the Boards the key conclusions reached from their research on the principles for derecognition of financial assets measured at fair value.

The Boards reinforced their objective of a common set of derecognition principles, however, no technical decisions were made.

#### IASB Observer Notes

KPMG International Financial Reporting Group has arranged to make available to KPMG member firms' clients and contacts copies of the IASB Observer, a publication of European Research Associates Limited. The IASB Observer provides timely, detailed reporting of IASB meetings. Please talk to your usual local KPMG contact to receive this publication.

If you would like further information on any of the matters discussed in this issue of *IFRS in Brief*, please talk to your usual local KPMG contact or call any of KPMG firms' offices.

KPMG International Financial Reporting Group is part of KPMG IFRG Limited.

KPMG International is a Swiss cooperative. Member firms of the KPMG network of independent firms are affiliated with KPMG International. KPMG International provides no client services. No member firm has any authority to obligate or bind KPMG International or any other member firm vis-à-vis third parties, nor does KPMG International have any such authority to obligate or bind any member firm.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

© 2007 KPMG IFRG Limited, a UK company, limited by guarantee. All rights reserved.

KPMG and the KPMG logo are registered trademarks of KPMG International, a Swiss cooperative.

Publication name: *IFRS in Brief*

Publication number: Issue 40

Publication date: November 2007