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Editorial

The comment period on the *Leases* exposure draft ended on 13 September 2013. The comments received by the IASB and the FASB are far from unanimous, and many criticisms have been expressed on both sides of the Atlantic, some even challenging the model upheld by the Boards. Even some organisations representing analysts or users of financial statements have suggested that the standard setters' proposals do not meet their needs.

Lively debates on this subject will therefore continue over the coming months, while, in parallel, work on the future of IFRSs goes on. The discussion paper reviewing the Conceptual Framework of IFRS, published in July 2013, is currently the subject of a series of events and webcasts throughout the comment period, which runs until January 2014. This month, Beyond the GAAP will introduce the key points.

Enjoy your reading!

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News

IAS 28: publication of draft amendments to IFRS for SMEs

On 3 October 2013, the IASB published an exposure draft presenting its proposed amendments to IFRS for SMEs, resulting from the first full review of this standard since its publication in July 2009.

In total, the IASB is proposing to amend 21 of its 35 chapters.

The suggested amendments are simple refinements or clarifications of the standard, and are unlikely to have any significant impact.

The comment period expires on 3 March 2014.

The exposure draft can be accessed on the IASB web site at: http://www.ifrs.org/IFRS-for-SMEs/ED-October-2013/Pages/Exposure-Draft-and-Comment-letters.aspx

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IFRS 9 Phase 2, Impairment: will the Boards converge?

At a joint meeting of the FASB and the IASB, the two Boards began the work of finalising their respective standards on the impairment of financial assets. It will be remembered that in summer 2012 the FASB opted for developing a distinct and ultimately very different approach to that hitherto developed in conjunction with the IASB. This divergence was reflected in the publication of two separate exposure drafts with very different approaches. Comments received by the Boards have been analysed over the summer.

Though a joint meeting was indeed held in September, at this stage both boards appear to be continuing to work on their own proposals. During this session, the IASB confirmed that the measurement objective for financial instruments for which there had been no significant decrease in credit quality since initial recognition ("stage 1 instruments") would continue to be 12-month expected credit losses. This is the point on which the IASB's view diverges most significantly from that of the FASB. For its part, the FASB took no tentative decisions on this issue during the September session. Discussions will resume in October.

Boards refine their positions on IFRS 9 Phase 1

The FASB and the IASB are continuing their debates in response to the comments received on their limited draft amendment to Phase 1 of IFRS 9, *Classification and measurement.* The September session was largely devoted to the 'solely payments of Principal and Interest' (P&I) condition which is to be met in order to measure for a financial asset at "amortised cost" or at "fair value through OCI". The exposure draft had confirmed that the cash flows on a financial asset should only represent repayments of principal and interest if this asset were to qualify for these two accounting categories. The Boards decided:

- that clauses with little impact on cash flows ("*de minimis* features") should be disregarded for classification;
- that the term "principal" refers to the amount transferred by the holder for the financial asset upon initial recognition;
- that the interest component consists primarily of consideration for the time value of money and credit risk, but these are not the only components that could be identified in a basic lending-type return. Other components of return consistent with the P&I condition, including the liquidity risk and profit margin, could also be identified;
- that regulated interest rates (those regulated by law, for example) could be used as a proxy for the consideration for the time value of money if those rates are not inconsistent with the basic lending-type relationship (no exposure to risks or volatility in cash flows, consideration consistent with the passage of time, etc.).

The two Boards also confirmed that contingent features (such as contingent prepayment or extension features) would not mechanically be considered as being inconsistent with the P&I condition, unless these features did not represent payments of principal or interest. The existence of a contingent feature therefore does not in itself prevent classification in the "amortised cost" or "fair value through OCI" categories. The profile of contingent cash flows should be analysed, along with the actual impact of the feature (is the feature genuine?).

Finally, the Boards also proposed specific provisions for assets acquired or originated with a significant premium or discount and containing a prepayment option at par value (and meeting some additional criteria) to enable them to be classified in categories other than "fair value through profit or loss".

IASB plans to amend some provisions of IAS 1

During its September meeting, the IASB discussed a number of projects relating to IAS 1, *Presentation of financial statements*, and has tentatively decided to amend it as follows:

- **Materiality and disclosures**

  The IASB proposes to clarify the concept of materiality and how it should be applied to disclosures, pointing out that disclosing immaterial information can adversely affect the readability of financial statements, by obscuring useful information.

- **Minimum contents of the statement of financial position and the statement of comprehensive income**

  The provisions of IAS 1 setting out the minimum contents of the statement of financial position and the statement of comprehensive income (paragraphs 54 and 82) will be amended to clarify that the required lines for these statements may be disaggregated to provide more detailed information, and that this must be done if doing so would provide more relevant information.

- **Presentation of OCI arising from equity-accounted investments**

  Following the proposal of the IFRS Interpretations Committee last July (see Beyond the GAAP no 69), the IASB decided to amend IAS 1 and its application guidance to clarify that other comprehensive income arising from entities accounted for using the equity method must be presented on a single line and not by nature, though retaining the distinction between items that will or will not be reclassified to profit or loss.

These issues should be dealt with in a single exposure draft, the publication of which is expected in Q1 2014.

IFRIC recommends the Board to amend IFRS 2

During its September 2013 meeting, the IFRS Interpretations Committee continued to deliberate on the question of share-based payment transactions in which the manner of settlement is contingent on a future event that is outside the control of both the entity and the counterparty (for example, a stock market listing).

During the meeting, the Committee observed that such share-based payment should be classified as either cash-settled or equity-settled in its entirety depending on which outcome is probable.

The Committee also decided that a change in the most likely settlement method should give rise to:

- a reclassification of the transaction in its entirety;
- the recognition of a cumulative adjustment, in such a way that the cumulative cost will be the same as if the arrangement had been classified in this way from inception.

On the basis of these conclusions, the Committee therefore recommended the IASB to amend IFRS 2.

IASB reviews the Conceptual Framework for IFRSs

In July 2013, the IASB published a discussion paper on the Conceptual Framework for Financial Reporting. The Conceptual Framework sets out the concepts that underlie the preparation and presentation of IFRS financial statements. Hence the importance of following the discussions in progress and of sending any comments to the IASB before 14 January 2014.

The discussions about the Conceptual Framework may seem esoteric. Nevertheless, they are important, for they affect the fundamental principles of IFRSs. The Conceptual Framework addresses the purpose of IFRS financial statements, their elements and their characteristics. It also contains definitions of assets and liabilities, income and expenses. It is used by the IASB in developing new or revising existing standards. Preparers of financial statements consider it when no IFRS specifically applies to a particular transaction or event.

➲ Why revise the Conceptual Framework?

The IASB has several reasons for updating the Conceptual Framework. Firstly, debates on current projects (including *Leases* and *Revenue recognition*) have exposed a need to clarify some fundamental principles, such as the definitions of performance or of assets and liabilities.

Next, the existing Conceptual Framework does not cover important topics such as the definition and presentation of OCI (other comprehensive income). Finally, in the course of the Agenda Consultation organised in 2011, the users of IFRS financial statements identified the revision of the Conceptual Framework as a priority project which should precede any new revision of IFRSs.

➲ What's in the IASB discussion paper?

Many subjects are tackled in its 238 pages. The following stand out:

Presentation of performance

The aim is to set out principles for the presentation of financial performance in the statement(s) of profit or loss and other comprehensive income (OCI). The IASB has restated its intention to retain a profit or loss total or subtotal and proposes to limit the use of OCI to items of income or expense resulting from certain remeasurements of assets and liabilities. The IASB also discusses the recycling of OCI in profit or loss.

Definitions of assets and liabilities

In the first analysis, it seems that more elements would meet the definition of an asset or a liability (however, see the discussion about the recognition of assets and liabilities below). As well as the concepts, the IASB provides application guidance to illustrate the issues raised by these definitions. In particular, section 3 of the discussion paper addresses the concepts of constructive obligation, economic compulsion and present obligation. The IASB notes that the existence of a present obligation is difficult to establish when the obligation is conditional and depends on the entity's future actions. An instance of this would be a variable contractual payment which is only due if the entity generates revenues in the future. The IASB identifies three alternative views for the recognition of these conditional obligations (with significant potential impacts on the recognition date of the corresponding liabilities).

Recognition / derecognition of assets and liabilities

The general principle set out in the discussion paper is that all assets and liabilities should be recognised (that is, every item meeting the definition of an asset or a liability). However, during the revision or development of any given standard, the IASB would have the latitude to decide that an entity need not, or should not, recognise an asset or a liability because :

- the recognition of these assets/liabilities would not provide relevant information to users of financial statements ; or
- no measure would result in a faithful representation of both the asset (or the liability) and the changes in the asset (or the liability).

Assets and liabilities would be derecognised when the recognition criteria no longer apply. However, the IASB has not at this stage decided how to recognise a residual involvement in a derecognised asset or liability.

Definitions of equity and financial liabilities and distinction between liability and equity elements

The IASB proposes to retain the existing definitions of equity and financial liabilities. 'Equity' would therefore continue to be defined as the residual interest in the assets of the entity after deducting all its liabilities. A financial liability would be defined as an obligation to deliver cash or another financial asset. The innovation here is that these definitions may be used to distinguish equity instruments from financial liabilities. So under this approach, obligations to issue equity instruments would meet the definition of equity instruments where the entity has no obligation to deliver cash. Under existing rules, obligations to issue equity instruments can meet the definition of a debt; an example would be an obligation to deliver a variable number of the issuer's equity shares or an equity derivative which does not respect the fixed-for-fixed rule.

Presentation of equity

Following on from the previous point, and the fact that more instruments would meet the definition of equity instruments, the IASB proposes to distinguish within equity between present claims on equity (for example the rights arising from holding ordinary shares) and future or potential claims on equity (for example rights arising from holding a share purchase warrant). As we understand it, this would mean distinguishing the claims of present shareholders from those of future (or potential) shareholders. The statement of changes in equity would provide information about transfers of wealth between current and future (or potential) shareholders using a measurement methodology as yet undecided, but which could be fair value.

What other matters are discussed?

The discussion paper also addresses the following:

- Principles regarding the choice of an appropriate measurement;
- Principles underpinning disclosures in financial statements and materiality;
- Significance of the business model in accounting for a transaction;
- Determining the unit of account;
- Going concern, stewardship, reliability and prudence.

What is the timetable for the review of the Conceptual Framework?

The IASB intends to move fast. The discussion paper published in July 2013 is an early draft ahead of the issue of an exposure draft in late 2014. The final text should be published by the end of 2015.

➲ What impact will this project have on existing IFRSs?

Current discussions will have no direct impact on the existing standards, at least in the short-term. The Conceptual Framework is not a standard and cannot be used to bypass the provisions of an IFRS. In the longer term, the review of Conceptual Framework will affect the development of new IFRSs and may have a knock-on effect in leading to a review of some existing standards to bring them into compliance with the new principles. Through the review of the Conceptual Framework, the face of future IFRSs is emerging before our eyes!

➲ How can you get involved in the debate?

All the project information and documents are public and can be consulted on the IASB web site. Everyone can respond to the IASB by sending a comment letter before 14 January 2014. You can also register for the events organised by the IASB. Note that EFRAG (the European technical organisation responsible for monitoring IFRS projects) is taking part in these discussions and has published a draft comment letter on its web site.

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The drafting of the present edition was completed on 20 October 2013

Frequently asked questions

IFRS

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- Accounting for the restructuring of a share purchase warrant;
- Setting up a capital increase programme through exercise of options;
- IFRS 10 analysis of a self-underwritten securitisation fund;
- First application of IFRIC 21;
- Classification of non-controlling interests in a fund with a finite life.

Upcoming meetings of the IASB, IFRS Interpretations Committee and EFRAG

IASB	Committee	EFRAG
23 Oct- 1 Nov 2013	12 - 13 November 2013	9 - 11 October 2013
14 - 22 November 2013	29 - 30 January 2014	6 - 8 November 2013
02 - 13 December 2013	25 – 26 March 2014	16 - 18 December 2013