

# Beyond the GAAP

No 52 – January 2012

It is already clear that 2012 will be a crucial year for the IASB. During the course of this year, the final texts of the joint projects on financial instruments, revenue recognition, leases and insurance contracts should all be published. Much is thus expected of the IASB.

Nevertheless, the new year has not started in top gear. January has been relatively quiet, and few important decisions have been taken at the Board's meetings. Only discussions in the IFRS Interpretations Committee (formerly IFRIC) on the accounting treatment of changes in the obligation due to sale options granted to non-controlling interests have shaken us out of the torpor of this severe winter.

Enjoy your reading!

Michel Barbet-Massin

Edouard Fossat

## Editorial

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## News

### New translations

The IFRS foundation has announced the publication of new translations in Finnish, Hebrew, Kazakh, French, Japanese and Spanish.

These official translations are accessible on the IASB web site, but remain reserved for the use of eIFRS subscribers.

### Three IASB members reappointed

On 24 January 2012, the Trustees of the IFRS foundation announced that they had reappointed three IAS members:

- Stephen Cooper (UK) and Wei-Guo Zhang (China) have both been appointed for a new 5 year term, running until 1 August 2017 and 30 June 2017, respectively.
- Paul Pacter (US) will extend his term of office by six months until 31 December 2012, to give the Trustees time to find his successor.

The Trustees have also announced that they are looking for three additional members to fill current and future vacancies.

### ➤ Leases: the two boards take a break

We have published no updates on the progress of the redeliberations on the leases project since October's newsletter. Nevertheless, the two boards have continued their work, mainly focusing on disclosures and the arrangements for first application.

This month, for the first time since the start of these redeliberations, the two boards have not discussed the leases project. However, a working group known as the "Leases Working Group Meeting" met on 24 January, and it appears that fundamental issues were discussed once again, for example the lease expense recognition profile in lessee's accounts.

To meet the needs of this working group, the IASB staff have produced a document summarising all the tentative decisions so far taken by the two boards.

This document can be consulted at the following address:  
<http://www.ifrs.org/NR/rdonlyres/2FB97651-39ED-43F4-975A-7E60B31DA8D4/0/WGP1SummaryofBoardscurrenttentativeDecisionsbytopic.pdf>

### ➤ Standards on consolidation: the IASB will not defer the effective date

In January 2012, the IASB studied the EFRAG request for the deferral of the effective date of IFRS 10, IFRS 11, IFRS 12, IAS 27R and IAS 28R to annual periods beginning on or after 1 January 2014 (see *Beyond the GAAP*, December 2011).

The Board unanimously decided not to defer the effective date beyond the date originally proposed, that is 1 January 2013.

The IASB observed that entities, including those in Europe, had already set in motion the resources required to apply these standards from 1 January 2013.

The IASB stated that it would have been inappropriate to defer the mandatory application of these texts when IFRS 10 and IFRS 12 form part of the Board's targeted response to the financial crisis.

In its draft opinion on the adoption of IFRS 10 and IFRS 11, published on its website on 9 February 2011, the EFRAG recommends that the European Commission set a mandatory effective date of 1 January 2014 while authorising early application.

### ➤ Early retirement programmes

The IFRS Interpretations Committee (formerly IFRIC) received a request for guidance regarding the application of IAS 19 to early retirement programmes. The issue submitted to the Committee specifically and exclusively concerned 'Altersteilzeit' plans (ATZ plans) in Germany.

ATZ plans are programmes designed to create an incentive for employees with a certain age group to smooth the transition from employment into retirement before the employees' legal retirement age. ATZ offer bonus payments in exchange for a 50 per cent reduction in working hours.

The issue was whether these bonuses should be treated as remuneration in exchange for services or as termination benefits.

Having observed that ATZ plans have attributes of both required service and termination benefits, the Committee noted that the distinction between benefits provided in exchange for services and termination benefits should be based on:

- all the relevant facts and circumstances;
- the indicators provided in paragraph 162 of IAS 19 as amended; and
- the definitions of the different categories of employee benefits in IAS 19.

The Committee noted that the fact that the bonus payments are wholly conditional upon completion of an employee service up to the legal retirement age indicates that the benefits are in exchange for that service.

Therefore, these bonus payments do not meet the definition of termination benefits.

### ➤ Reopening of Phase 1 of IFRS 9: Classification and measurement

The IASB and the FASB have confirmed their desire to improve the alignment of their respective models for the classification and measurement of financial instruments.

With this in view, the two boards have identified the aspects which they would like to address:

## IFRS

- the way in which the contractual cash flow characteristics of an instrument are taken into account in the classification process;
- the need to reintroduce the concept of embedded derivatives that may be bifurcated for financial assets;
- the basis for and scope of a possible third classification category of financial assets (debt instruments measured at fair value through other comprehensive income) ;
- any knock-on effects from the above, including disclosures.

### ➤ Impairment of financial assets – proposal of a specific treatment for assets purchased with an explicit expectation of credit losses at the acquisition date

During the joint meeting on 27 January 2012, the FASB and the IASB presented the main features of the impairment model to be applied to a very specific category of financial assets: purchased financial assets with an explicit expectation of credit losses at acquisition.

- These assets would be classified initially in buckets 2 or 3 and presented on the balance sheet at their purchase price: this is therefore an exception to the treatment of originated assets, which would be consistently initially classified in bucket 1;
- no impairment loss would be recognised on acquisition;
- any subsequent increase in losses expected over the residual lifetime of the instrument would be recognised as an impairment loss in profit or loss for the period;
- in the event of an increase in cash flows expected to be collected, the differential would be accounted for immediately in profit or loss.
- disclosures may be required on the amount of expected losses that are implicit in the purchase price.

## European matters

### ➤ EFRAG publishes its draft endorsement advice(s) on the new standards on consolidation

On 9 February 2012, EFRAG published its draft endorsement advice on IFRS 10, IFRS 11, IFRS 12 and the consequent amendments to IAS 27 and IAS 28.

Unsurprisingly, EFRAG consider that the new standards meet the endorsement criteria. Notwithstanding this positive recommendation on endorsement criteria, EFRAG does not support the effective date of 1 January 2013.

Given the tardy publication of the standards, and of two associated projects in progress (*ED/2011/4 Investments Entities* and *ED/2011/7 Transition Guidance: Proposed amendments to IFRS 10*), EFRAG believes that entities will not have sufficient time to get to grips with these standards and that it is impossible to develop a common understanding of these standards in so short a period. These difficulties have been confirmed by field-tests conducted in recent weeks.

Stakeholders' comment on the EFRAG draft advice should be submitted on or before 11 March 2012.

The full invitation to comment can be consulted at <http://www.efrag.org/Front/n1-904/EFRAG-requests-comments-on-its-draft-endorsement-advice-s--and-draft-effects-study-report-s--on-IFRS-10--IFRS-11--IFRS-12--IAS-28--2011--and-IAS-27--2011-.aspx>

### ➤ EFRAG publishes a Discussion Paper on Business Combinations under Common Control

At the end of 2011, EFRAG published a Discussion Paper (DP) on Business Combinations under Common Control.

Readers will recall that the IFRSs do not address the accounting treatment of business combinations under common control. These are explicitly excluded from the scope of IFRS 3 on Business Combinations.

In practice, and in the absence of any guidance in IFRS 3 as to the accounting treatment of these combinations, a range of approaches are applied by accounts preparers, principally:

## European matters

- the acquisition method applicable to transactions where an acquirer obtains control of one or more businesses;
- the historical book value method.

The aim of the DP is to enter into a debate about the way these transactions should be measured and accounted for in the acquirer's financial statements.

Comment letters may be submitted to EFRAG until 30 April 2012.

Further details of the Discussion Paper can be found at:  
<http://www.efrag.org/Front/p157-2-272/Proactive---Business-Combinations-under-Common-Control.aspx>

### ➤ EFRAG publishes a Discussion Paper on accounting for corporate income taxes

At the end of the year, EFRAG published a Discussion Paper for feedback on the accounting for corporate income taxes.

The current standard on income taxes (IAS 12) appears to be the subject of some debates about the practical aspects of its application.

The aim of the DP is to stimulate discussions on accounting for income taxes:

- a first part devoted to areas which require clarification in order to make the existing standard more straightforward. Examples include the reconciliation of tax expense to a standard rate, requirements in respect of uncertain tax positions and whether deferred tax should be discounted.
- a second part addressing alternative approaches to accounting for income taxes. This second part could serve as the starting point for a new standard which would replace IAS 12.

Comment letters on this DP may be submitted to EFRAG until 29 June 2012.

For more details of the document, please consult:  
<http://www.efrag.org/Front/p177-2-272/Proactive---Financial-Reporting-for-Corporate-Income-Taxes.aspx>

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## Puts on non-controlling interests (NCI): the Committee recommends recognition of changes in P&L

At its recent meeting on 17 and 18 January 2012, the IFRS Interpretations Committee (formerly IFRIC) continued its discussions of the accounting treatment of changes in the debt due to sale options granted to non-controlling interests in subsidiaries ("NCI puts"). Beyond the GAAP presents the Committee's latest approach to this very sensitive topic.

### ➤ What accounting treatment applies today?

It should be remembered that the entity's obligation to purchase non-controlling interests benefiting from sale options means that a liability must be recorded in the IFRS consolidated accounts, the debt being recognised at the present value of the estimated purchase price.

For subsequent changes in the debt, two approaches have historically been applied:

- An approach based on IAS 39, which consists in recognising changes in the debt in profit or loss (on the basis that IAS 32 refers to the provisions of IAS 39 for the subsequent recognition of the debt, and that changes in the debt must be recognised in profit or loss under IAS 39).
- An alternative approach based on IAS 27R, which consists in recognising changes in the debt in equity (on the basis that transactions with non-controlling interests should be analysed as transactions between shareholders where they do not affect the exclusive control exercised by the entity).

In its recommendations for the 2009 reporting period, the French market regulator ("AMF") accepted both methods, though it expressed a preference for the equity approach.

### ➤ What is at stake?

In the event, frequent in practice, that the exercise price is based on fair value at the exercise date, it is at the very least counter-intuitive to account for increases in the debt in P&L, when it is the sound management of the entity by the controlling shareholder that is responsible, and when the purchase price is a 'normal' price.

In other words, the normally-priced purchase, offering a simple exit route to a non-controlling shareholder (effectively, a guarantee of liquidity), results in impacts on the entity's result where it has entered into a contract (i.e. the entity granted a put).

In contrast, a straightforward purchase, at the same price but without prior commitment, results in an impact on equity (i.e. without any impact on profit or loss).

### ➤ What was proposed in the draft IAS 32 amendment?

In March 2011, the IFRS Interpretations Committee (formerly IFRIC) examined a draft amendment to IAS 32. This draft amendment (see Beyond the GAAP of March and September 2011) proposed that sale options with certain precise characteristics:

- should be excluded from the scope of IAS 32, and
- should therefore be accounted for in accordance with IAS 39, as derivative instruments.

In practice, the measurement of puts in accordance with IAS 39 (i.e. as derivatives) would result in the disappearance of

the liability (as such, though this would not stand in the way of recognition of a derivative liability) and all changes in fair value would be accounted for in profit or loss.

However, the IASB did not want to amend the scope of IAS 32, though it did wish to clarify the accounting treatment of subsequent variations in the debt.

## ➤ What approach was taken by the Committee?

At its January 2012 meeting, the Committee decided that the 'financial instrument' approach, in which changes in the obligation should be accounted for in profit or loss, was preferable.

- The Committee noted that paragraph 30 of IAS 27 on changes in ownership interest does not apply to NCI puts insofar as the ownership interest is not changed before any exercise of the put by the non-controlling interest shareholder.
- The put requires the recognition of a financial liability and its remeasurement does not change the respective ownership interests of the controlling shareholder or the non-controlling interest shareholder.

However, before making its recommendation to the board, the Committee would like to ensure that it has no unintended consequences on related aspects of the accounting for NCI puts, including initial recognition of the NCI put or general consolidation mechanics

## ➤ What are we to make of this decision?

While we can welcome the fact that the technical discussions around puts, begun by the former IFRIC in 2005, seem to be approaching a conclusion, we nevertheless regret that the proposal for a scope amendment of IAS 32 has not been accepted by the IASB.

Even though the Committee's position is understandable in technical terms, the accounting treatment suggested does not seem to reflect adequately the particular nature of NCI puts, which fall somewhere between IAS 32 and IAS 27.

The approach suggested by the Committee implicitly assumes that this debt is a normal liability, whereas the failure to exercise the option by the non-controlling interest leads, in accounting terms, to the cancellation of the debt through shareholders' equity (and not in profit or loss, as in the case of a "normal" liability).

Finally, from the point of view of readers of financial statements, the mechanistic approach preferred by the Committee is difficult to understand, and will require a good measure of education.

We will not fail to report on further developments on this sensitive subject.



## Events/publications

### Seminars on "Current developments in IFRS"

Throughout 2012, Mazars' Doctrine team will lead a number of seminars on IFRSs.

These seminars, organised by Francis Lefèbvre Formation, will take place on 23 March, 22 June, 21 September and 7 December 2012.

Applications for registration should be sent to: Francis Lefèbvre Formation : [www.flf.fr](http://www.flf.fr) or 01 44 01 39 99.

## Frequently asked questions

### IFRS

- Allocation of free shares: from what point must the past services of the employee be recognised?
- Critical event for revenue recognition when the delivery of goods is delayed at the customer's request.
- Evaluation of customer loyalty programmes (IFRIC 13).
- Accounting treatment of energy economy certificates (EEC).
- How to treat intra-group operations in the presentation of discontinued operations?

## Upcoming meetings of the IASB, IFRS Interpretations Committee and EFRAG

### IASB

27 - 29 February 2012

19 - 23 March 2012

16 - 20 April 2012

### Committee

13 - 14 March 2012

15 - 16 May 2012

10 - 11 July 2012

### EFRAG

22 - 24 February 2012

20 - 21 March 2012

2 - 4 April 2012

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