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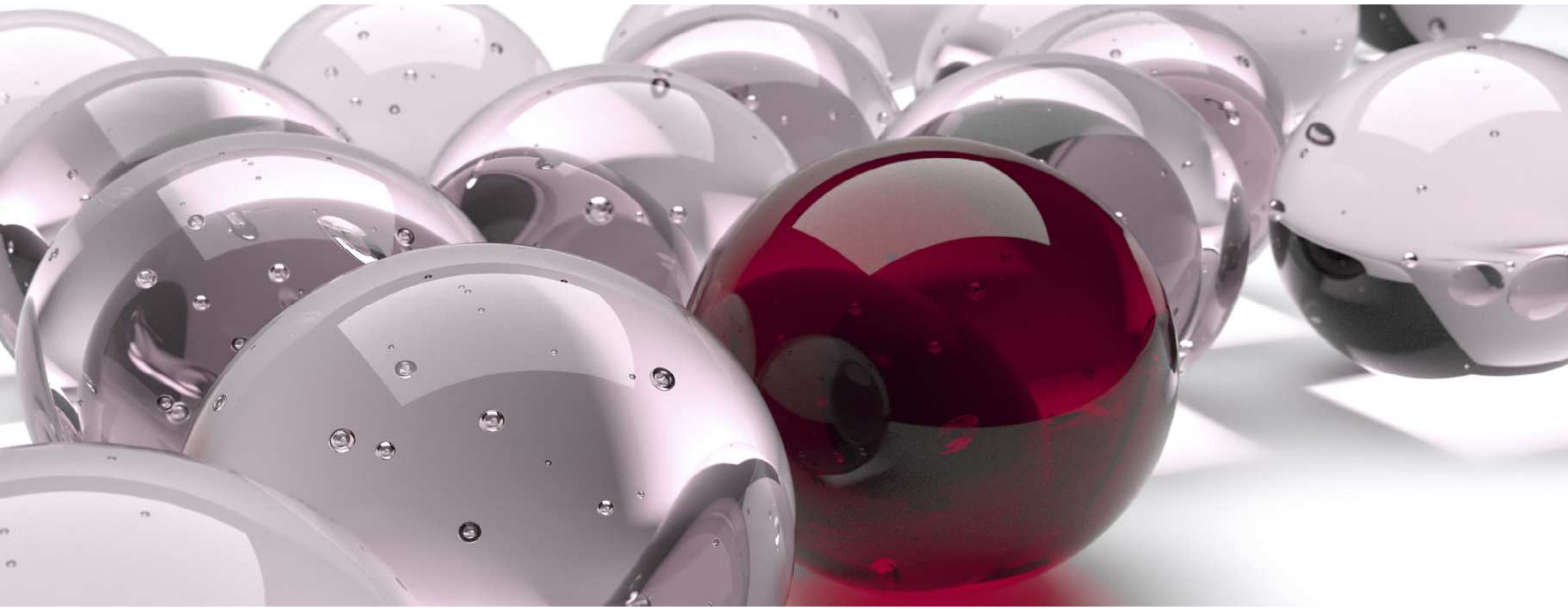
Beyond the GAAP

Mazars' newsletter on accounting standards



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EDITORIAL

At last! Between the publication in December 2008 of the Discussion Paper on Revenue Recognition, and the arrival of IFRS 15 at the end of May 2014, nearly five and a half years have passed. During this period, two exposure drafts were published (June 2010 and November 2011), and it took 30 months' work to move from the second exposure draft to the final joint standard with the US GAAP.

Despite this delay in publishing the standard, the mandatory application date is still 1 January 2017. Let us hope that this period will be sufficient for the Transition Resource Group, set up jointly by the IASB and the FASB, to identify and analyse any application difficulties that IFRS 15 may pose. Recent experience of the standards on consolidation - IFRS 11 in particular - that are currently dominating the agenda of the IFRS Interpretations Committee has shown the importance of dealing with application problems at an early stage.

A future edition of Beyond the GAAP will introduce the provisions of IFRS 15. In the meantime, this issue contains a selection of the recent decisions taken by the IASB and the IFRS IC.

Enjoy your reading!

Michel Barbet-Massin Edouard Fossat

News

IFRS Foundation publishes its 2013 annual report

On 22 May 2014, the IFRS Foundation published its Annual Report for the year ended 31 December 2013. As well as containing a financial section, the report, entitled *Charting progress towards global accounting standards* outlines the work of the IFRS foundation and the use of IFRSs around the world, and reports on the year's standard-setting activities.

The report can be consulted at http://www.ifrs.org/The-organisation/Governance-and-accountability/Annual-reports/Pages/2013-Annual-Report.aspx

SEC reiterates its wish to see IFRSs adopted in the US, but sets no timetable

At the annual dinner of the Financial Accounting Foundation, SEC chairman Mary Jo White spoke again of the importance of achieving the international convergence of accounting principles, and said that the incorporation of IFRSs in the US standards was among her priorities.

Nevertheless, the incorporation of IFRSs in US standards seems conditional on the preservation of certain interests of investors and American standard-setting bodies. Mrs White said the following three things:

- first, the interests of U.S. investors would remain 'front and centre';
- second, the FASB would remain 'front and centre' as the ultimate standard setter of accounting standards for U.S. companies;
- and third, the role the United States plays in the development of global standards must be an important consideration.

The chairman concluded her remarks by noting that the US, and more particularly the SEC, must respond in the near future to the questions posed by international regulatory and accounting bodies. Although no timetable was set, the SEC would have to determine the issue of further incorporation of IFRS into the US capital markets.

Hans Hoogervorst discusses the IASB work programme

On 29 May 2014 at the IFRS conference in Singapore Hans Hoogervorst, Chairman of the IASB, discussed the board's work plan.

After talking about the successful spread of IFRSs in the past ten years, the Chairman stressed the need for the continuous development of the standards, and focused on the following major topics:

- Revenue recognition, the recent subject of a newly published standard converging IFRS and US GAAP;
- Accounting for leases, which the Chairman described as a vast project. To make it easier to apply the standard, the board had decided to exclude certain leases, such as short-term leases and those with variable lease payments. Discussions between the FIASB and the FASB were ongoing, and the work should be finalised within the next couple of months;
- IFRS 9 – *Financial instruments,* the new version of which should be published in July. The Chairman highlighted improvements relating to the 'own credit' risk problem and loan loss provisioning (the move from an incurred loss to an expected loss model);
- Disclosure overload, which had already led to some amendments to IAS 1 last March. Immaterial information should be avoided if it threatens to overshadow material information

The Chairman concluded by mentioning the next stages of the disclosures project, including a study of how materiality is used in practice project to harmonise the principle of disclosure across the existing IFRSs.

The full text can be consulted at: http://www.ifrs.org/The-organisation/Members-of-the-IASB/IASB-speeches/Documents/2014/Hans-Hoogervorst-speech-IFRS-Singapore-May-2014.pdf

IFRS Highlights

IFRS 7 disclosures on the transfer of financial assets

At its meeting of May 2014, the IFRS IC analysed the comment letters received regarding the amendment of IFRS 7 on the transfer of financial assets that was included in the 2012-2014 *Annual improvements*.

The initial draft proposed to clarify that servicing agreements carried out by the transferor would generally be considered as continuing involvement under IFRS 7. The board's position rested on the assumption that servicing agreements generally represent variable remuneration reflecting the performance of the transferred assets.

During its May 2014 deliberations the IFRS IC decided to drop this assumption, which many stakeholders believed to be unfounded (particularly where remuneration is fixed and independent of the performance of the transferred assets), and to clarify that the term 'continuing involvement' in IFRS 7 is used in a different way from that term in IAS 39.

IASB work plan

At the end of its May 2014 meeting, the IASB updated its work plan. Notable announcement include:

- the discontinuation of the draft narrow-scope amendment to IAS 28 *Equity Method: Share of Other Net Asset Changes*; and
- the postponement of the publication of amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets Between an Investor and its Associate or Joint Venture* to Q3 2014.

The IASB work plan can be consulted on the IASB site at: http://www.ifrs.org/Current-Projects/IASB-Projects/Pages/IASB-Work-Plan.aspx

IASB and FASB set up a joint IFRS 15 transition group

On 3 June 2014, the IASB and the FASB announced that they were setting up a group to oversee the application of the new IFRS 15 *Revenue recognition*

The Transition Resource Group (TRG) will be made up of preparers, auditors and users of financial statements. Its role will be to inform the IASB and the FASB about implementation issues that may arise for entities applying IFRS 15, though it will not issue technical guidance.

The boards expect that the TRG will meet six times, twice in 2014 and four times in 2015. The first meeting is scheduled for 18 July 2014.

For more about the TRG, including details of how to submit a question, see the IASB press release at: http://www.ifrs.org/The-organisation/Advisory-bodies/Joint-Revenue-Transition-Resource-Group/Pages/Home.aspx

IASB and FASB publish new Revenue Recognition standard, at last

On 28 May 2014, the IASB and the FASB published a new converged standard on revenue recognition. This publication is the culmination of years of work. The aim is to provide entities using IFRSs with a more robust and comprehensive standard covering all transactions, even the most complex, without further need to consult another body of standards or to develop interpretation guidance. The boards have also sought to enhance the relevance of disclosures.

IFRS 15 (ASU 2014-09 in the US) sets out the revenue recognition principles applicable to all contracts with customers (except leases, insurance contracts and contracts covered by the standards on financial instruments). In practice, IFRS 15 replaces IAS 18 on revenue and IAS 11 on construction contracts (and all the linked interpretations: IFRIC 13, IFRIC 15, IFRIC 18 and SIC 31).

IFRS 15 clarifies when an entity must recognise revenue, and for what amount. The standard uses a five-step model:

- Step 1: Identify the contract with the customer;
- Step 2: Identify the separate performance obligations in the contract;
- Step 3: Determine the transaction price of the contract;
- Step 4: Allocate the transaction price to the separate performance obligations;
- Step 5: Recognise the revenue when (or as) a performance obligation is satisfied.

Application guidance (covering issues such as performance obligations satisfied over time, or sales with a right of return), is appended to IFRS 15, and illustrative examples are also provided.

IFRS 15 will be of mandatory application for reporting periods beginning on or after 1 January 2017, subject to endorsement by the European Union. Earlier application is permitted. The transitional provisions state that initial application should be retrospective, but with significant reliefs where entities elect to recognise the impact of the change of method at 1 January 2017 for contracts that are not completed contracts at that date (i.e. no restatement of the comparative periods presented in such a case).

Beyond the GAAP will shortly publish an analysis of the main provisions of IFRS 15 and an overview of the significant anticipated impacts.

IFRS IC continues to examine the liability/equity classification of specific instruments mandatorily convertible into shares

The IFRS Interpretations Committee is continuing its discussion on issued instruments that are mandatorily convertible into shares (see Beyond the GAAP no 75), and at its May meeting considered the accounting classification under IAS 32 of an instrument with the following characteristics:

- The financial instrument has a stated maturity date and, at maturity, the issuer must deliver a variable number of its own equity instruments to equal a fixed cash amount. This variable number of equity instruments is nevertheless subject to a cap and a floor.
- The instrument carries interest at a fixed rate and the payment of this interest is mandatory.

The question submitted to the Committee was whether an equity component could be identified within this instrument, corresponding to the minimum number of shares set by the floor that the issuer was certain to deliver.

The Committee confirmed the tentative decision taken in January's meeting according to which the obligation to redeem the instrument in shares should not be subdivided into several components (i.e. an equity component corresponding to the floor threshold, and another component reflecting the variability of the number of shares to be delivered). Rather, the Committee believed that the instrument should be analysed as a whole. The Committee decided that the contractual substance of the instrument was a single obligation to deliver a variable number of equity instruments at maturity, and that as a consequence the entire obligation met the definition of a financial liability.

Consequently, the embedded feature of redemption in shares constitutes a derivative under IAS 39 (and under IFRS 9) that is not closely related to the host liability contract and should therefore be accounted for separately (assuming that the issuer has not elected to designate the entire instrument under the fair value option).

Demise of the project to clarify the accounting treatment of "other net asset changes" in an associate or joint venture

On 22 November 2012 the IASB published a draft amendment to IAS 28, aiming to clarify the investor's accounting treatment of its share of other net asset changes in the investee (i.e. other than the result of the investee, other comprehensive income and the dividends paid by the investee).

With this project the IASB proposed to recognise in the investor's equity its share of the changes in the equity of the investee that are linked with the other variations and to reclassify in P&L, when significant influence is lost, the amounts previously accounted for in equity in accordance with the new proposals (see Beyond the GAAP of November 2012).

The comment letters were somewhat critical. In July 2013 the Interpretation Committee recalled its initial proposals, namely to treat reductions in the interest percentage as partial disposals and increases in the interest percentage as supplementary acquisitions (see Beyond the GAAP, July-August 2013).

However, in December 2013, the IASB decided that none of the approaches under consideration were without problems and decided to finalise its proposals. It acknowledged that this was only a short-term solution to put an end to the diverse practices until the Board could look again at the principles of the equity method.

During the March 2014 meeting the IASB had decided that it would not be necessary to re-expose the amendment, and that it would become mandatory for financial years starting on or after 1 January 2016. It did not mention at this stage the possibility of early application of the amendment (see Beyond the GAAP of March 2014).

In the light of the increasing opposition within the board, and the impossibility of commanding a majority in favour of this amendment, the board finally decided not to pursue this project at its May meeting.

Acceptable methods of amortisation

In the November 2013 issue of Beyond the GAAP we reported the IASB's decision to go ahead with the amendments proposed in the exposure draft ED/2012/5 *Clarification of Acceptable Methods of Depreciation and Amortisation* (amendments to IAS 16 and IAS 38), mainly aiming to:

- prevent the use of revenue-based methods for tangible assets in IAS 16,
- introduce a rebuttable presumption in IAS 38 that such depreciation methods are inappropriate for intangible assets.

This has now been done, since the IASB has published the amendments to IAS 16 and IAS 38 on acceptable methods of depreciation or amortisation.

These amendments shall be applied prospectively for annual periods beginning on or after 1 January 2016. Earlier application is permitted (subject to adoption by the European Union).

Leases: further redeliberations

The FASB and the IASB continued to redeliberate the proposals in the draft standard on leases, which was the subject of a second exposure draft on 13 May 2013.

During their joint meeting in May, the two boards discussed the following areas:

- Definition of a lease
- Separation of the lease and non-lease components of a contract
- Initial direct costs.

The decisions taken by the two boards during this meeting essentially consisted of clarifications and simplifications of the model proposed in the May 2013 exposure draft.

Beyond the GAAP will present a detailed account of the decisions taken at this meeting once all the two boards' redeliberations are sufficiently advanced.

EUROPEAN Highlights

ESMA report on the activities of IFRS Enforcers in Europe

ESMA (the European Securities and Markets Authority) has just published a report on the activities of European regulators.

The report reveals that:

- European enforcers performed full reviews of around 1050 interim and annual IFRS financial statements, representing around 14% of listed entities in Europe,
- Around 850 financial statements were subject to partial review, representing coverage of 11 % of the population of listed entities.

The report also mentions the *a posteriori* review of 185 2012 financial statements in the light of the ESMA's 2012 recommendations published on 12 November 2012 (ESMA/2012/725). As a result of this evaluation national enforcers took 46 enforcement actions:

- 16 issuers were required to publish a correction;
- 30 required corrections in future financial statements.

Readers will recall that these 2012 recommendations, issued against the background of crisis, focused on areas such as the impairment of non-financial assets, defined benefit obligations, and provisions for non-financial liabilities (for more details on these 2012 recommendations see Beyond the GAAP of November 2012).

The ESMA activity report can be consulted at: http://www.esma.europa.eu/system/files/2014-551_activity_report_on_ifrs_enforcers_in_europe_in_2013.pdf

A Closer Look

The IASB clarifies the accounting for acquisitions of interests in joint operations

The IASB has just published amendments to the standard IFRS 11 – *Joint Arrangements*. Readers will remember that IFRS 11 establishes principles for financial reporting by entities that have an interest in arrangements that are controlled jointly (i.e. joint arrangements). IFRS 11 classifies joint arrangements into two types:

- joint ventures, which are consolidated by the joint venturers using the equity method;
- Joint operations, where the joint operators account for their share of the assets, liabilities, revenue and expenses.

The amendments now published by the IASB clarify the accounting for the acquisition of an interest in a joint operation that constitutes a business (as defined in IFRS 3 – *Business combinations)*. These transactions are relatively uncommon except in certain business sectors (in particular the oil sector).

The amendments state that the principles on business combinations accounting in IFRS 3, and other IFRSs, should be applied to these transactions to the extent of the investor's share, as long as they do not conflict with the guidance in IFRS 11. Consequently, when an entity acquires an interest in a joint operation in which the activity of the joint operation constitutes a business (as defined in IFRS 3), it must:

- measure identifiable assets and liabilities at fair value (other than items for which exceptions are given in IFRS 3 and other IFRSs);
- recognise acquisition-related costs (e.g.. fees paid to consultants, valuers, etc.) as expenses, with the exception that the costs to issue debt or equity securities are recognised in accordance with IAS 32/IAS 39;
- recognise deferred tax assets and liabilities that arise from the initial recognition of assets or liabilities (except for deferred tax liabilities that arise from the initial recognition of goodwill), as required by IFRS 3 and IAS 12;
- recognise goodwill equal to the excess of the consideration transferred over the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed;
- apply the provisions of IAS 36 relating to impairment tests of goodwill.

It is no longer possible to account for these transactions as acquisitions of separate assets by allocating the acquisition cost to the individual identifiable assets on the basis of their relative fair values at the date of purchase (which resulted in no recognition of goodwill, or deferred tax assets and liabilities and the capitalisation of the acquisition-related costs).

These amendments also apply to the formation of a joint operation if an existing business, as defined in IFRS 3, is contributed to the joint operation by one of the parties that participate in the joint operation. However, these amendments do not apply to the formation of a joint operation if all of the parties that participate in the joint operation only contribute assets or groups of assets that do not constitute businesses (as defined in IFRS 3) to the joint operation on its formation (i.e. if the parties contribute assets which form a business when brought together).

The amendments also clarify that if a joint operator increases its interest in a joint operation in which the activity constitutes a business as defined in IFRS 3 by acquiring an additional interest in the joint operation, the previously held interests in the joint operation are not remeasured at the time of the additional acquisition if the joint operator retains joint control (i.e. there is no impact in P&L due to the additional acquisition).

Finally, these amendments do not apply on the acquisition of an interest in a joint operation when the parties sharing joint control, including the entity acquiring the interest in the joint operation, are under common control of the same ultimate controlling party or parties both before and after the acquisition (consistently with the provisions in IFRS 3 for business combinations under common control).

An entity shall apply those amendments prospectively for annual periods beginning on or after 1 January 2016, subject to endorsement by the European Union. Earlier application is permitted.

A Closer Look

Standards and interpretations applicable at 30 June 2014

To coincide with the preparation of interim financial reports, Beyond the GAAP presents an overview of the IASB's most recent publications. For each text, we clarify whether it is mandatory for this closing of accounts, or whether early application is permitted, based on the EU endorsement status report (Position as at 12 May 2014): http://www.efrag.org/WebSites/UploadFolder/1/CMS/Files/Endorsement%20status%20report/EFRAG_Endorsement_Status_Report_12_May_2014.pdf

As a reminder, the following principles govern the first application of the IASB's standards and interpretations:

- The IASB's draft standards cannot be applied as they are published standards.
- IFRIC's draft interpretations may be applied if the two following conditions are met:
  - The draft does not conflict with currently applicable IFRSs;
  - The draft does not modify an existing interpretation which is currently mandatory.
- Standards published by the IASB but not yet adopted by the European Union may be applied if the European adoption process is completed before the interim financial reports have been approved by the relevant authority (i.e. usually the board of directors).
- Interpretations published by the IASB but not yet adopted by the European Union at the end of the interim financial reporting period may be applied unless they conflict with standards or interpretations currently applicable in Europe.

It should also be noted that under IAS 34 "Interim Financial Reporting", the changes in accounting policies required for 2014 by new standards must also be disclosed in the interim financial reporting published during the course of the year.

1. Situation of European Union adoption process for standards and amendments published by the IASB

<table>
<tr><th>Standard</th><th>Subject</th><th>Effective date according to IASB</th><th>Date of publication in the Official Journal</th><th>Application status on 30 June 2014</th></tr>
<tr><td>IFRS 10</td><td>Consolidated Financial Statements</td><td rowspan="5">1/01/2013
Early application permitted if all these Standards are applied at the same time</td><td rowspan="5">29 December 2012
Mandatory to financial year starting on 01/01/2014</td><td rowspan="5">Mandatory</td></tr>
<tr><td>IFRS 11</td><td>Joint Arrangements</td></tr>
<tr><td>IFRS 12</td><td>Disclosures of interests in Other Entities</td></tr>
<tr><td>IAS 27R</td><td>Separate Financial Statements</td></tr>
<tr><td>IAS 28R</td><td>Investments in Associates and Joint Ventures</td></tr>
<tr><td>Amendments to IFRS 10, IFRS 11 year IFRS 12</td><td>Transition Guidance</td><td>1/01/2013
Early application Permitted</td><td>5 April 2013
Mandatory to financial year starting on 01/01/2014</td><td>Mandatory</td></tr>
<tr><td>Amendments to IFRS 10, IFRS 12 and IAS 27</td><td>Investment Entities</td><td>1/01/2014
Early application permitted</td><td>21 November 2013</td><td>Mandatory</td></tr>
<tr><td>Amendments to IAS 32</td><td>Presentation – Offsetting Financial Assets and Financial Liabilities</td><td>1/01/2014
Early application Permitted</td><td>29 December 2012</td><td>Mandatory</td></tr>
<tr><td>Amendments to IAS 36</td><td>Recoverable Amount for Non-Financial Assets</td><td>1/01/2014
Early application permitted</td><td>20 December 2013</td><td>Mandatory</td></tr>
<tr><td>Amendments to IAS 39</td><td>Novation of Derivatives and Continuation of Hedge Accounting</td><td>1/01/2014
Early application permitted</td><td>20 December 2013</td><td>Mandatory</td></tr>
</table>

1. Situation of European Union adoption process for standards and amendments published by the IASB (continued)

Standard	Subject	Effective date agreement to IAS	date of publication i the Official log	Application status on 30 June 2014
Annual improvements to IFRS 2010-2012	Annual improvements to various Standards *(issued on 17 December 2013)*	**1/07/2014** Early application permitted	Awaiting endorsement by the EU (expected in Q4 2014)	**Permitted** [1]
Annual improvements to IFRS 2011-2013	Annual improvements to various Standards *(issued on 17 December 2013)*	**1/07/2014** Early application permitted	Awaiting endorsement by the EU (expected in Q4 2014)	**Permitted** [1]
Amendments to IAS 19	Employee Contributions *(issued on 21 November 2013)*	**1/07/2014** Early application permitted	Awaiting endorsement by the EU (expected in Q4 2014)	**Permitted** [1]
IFRS 9	Financial Instruments (standard intended to gradually replace the provisions of IAS 39)	**Undetermined** Should be decided upon when the entire IFRS 9 project is closer to completion. Early application permitted	Endorsement postponed	**Not permitted**
Amendments to IAS 16 year IAS 38	Clarification of Acceptable Methods of Depreciation and Amortisation (*issued on May 2014*)	**1/01/ 2016** Early application permitted (prospectively)	Awaiting endorsement by the EU (expected in Q1 2015)	**Permitted** [1]
Amendments to IFRS 11	Accounting for Acquisitions of Interests in Joint Operations *(issued on 6 May 2014)*	**1/01/ 2016** Early application permitted	Awaiting endorsement by the EU (expected in Q1 2015)	**Not permitted**

[1] If the amendment is a clarification of an existing standard and is not in contradiction with current standards

2. Situation of European Union adoption process for interpretations published by the IASB IFRS IC

Interpretation	Subject	Effective date agreement to IAS	date of publication i the Official log	Application status on 30 June 2014
IFRIC 21	Levies (issued on 20 May 2013)	**1/01/2014** Early application permitted	Awaiting endorsement by the EU (expected in Q2 2014)	**Permitted**

Events year FAQ

Frequently asked questions

IFRSs

- Taking account of tax-loss carry forwards in the effective tax rate method applicable in interim statements (IAS 34)
- Disclosures to be presented regarding the changes of methods resulting from the first application of the consolidation standards (IFRS 10, IFRS 11, IFRS 12, IAS 28R).
- Accounting for a share-based payment transaction (IFRS 2) that is cash-settled and includes a guaranteed minimum.
- Ways of applying the transitional arrangements for the new consolidation standards and presentation of the change of methods in the half-yearly financial statements.
- Identification of the triggering event for the reversal of impairment of investments in equity affiliates.

Upcoming meetings of the IASB, IFRS Interpretations Committee and EFRAG

IASB	Committee	EFRAG
13 - 20 June 2014	15 - 16 July 2014	11 - 13 June 2014
17 - 25 July 2014	16 - 17 September 2014	14 - 16 July 2014
18 - 25 September 2014	11 - 12 November 2014	3 - 5 September 2014