

IFRS in Brief

July 2008, **Issue 48**

This issue of IFRS in Brief covers the June 2008 meeting of the International Accounting Standards Board (IASB or Board).

Summary

At its June 2008 meeting the IASB continued discussing the:

- proposed amendments to IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*
- proposed amendments for the next annual improvements exposure draft (ED)
- conceptual framework project
- extractive activities research project
- fair value measurement project
- financial statement presentation project
- ED of *Proposed Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Exposures Qualifying for Hedge Accounting*
- ED of an *IFRS for Private Entities* (previously *IFRS for Small and Medium-sized Entities*).

In addition, at its June 2008 meeting the IASB:

- discussed recent International Financial Reporting Interpretations Committee (IFRIC) activities

- reviewed a report from the first meeting of the valuation expert advisory panel
- reviewed the technical plan.

Proposed Amendments to IFRS 5

The Board reviewed whether the definition of discontinued operations should include subsidiaries that on acquisition meet the criteria to be classified as held for sale. The Board decided, for components of an entity either disposed of or classified as held for sale, that:

- if any disclosure exemptions are provided to such subsidiaries, then similar exemptions also would need to be provided in the business combination requirements
- it would not prescribe whether the disclosures could be aggregated
- the use of proceeds would not be a required disclosure.

Annual Improvement Process

As part of its second annual improvements ED, expected to be published in August 2008, the Board considered three proposed improvements to amend:

- IAS 7 *Statement of Cash Flows* to clarify that only expenditures that result in a recognised asset would be classified as cash flows from investing activities

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

- IAS 36 *Impairment of Assets* to clarify that when allocating goodwill arising from a business combination to cash-generating units or a group of cash-generating units, the largest unit permitted for impairment testing would be the lowest level of operating segment as defined in IFRS 8 *Operating Segments*, prior to the impact of the IFRS 8 aggregation criteria
- IFRS 2 *Share-based Payment* to clarify that the formation of a joint venture and common control transactions would be specifically excluded from the scope of IFRS 2.

Conceptual Framework Project

The Board discussed two topics as part of its deliberations of the conceptual framework project *Phase B: Elements and recognition*.

Statutes, Laws and Regulations

In considering whether statutes, laws and regulations give rise to a liability, the Board tentatively decided that an entity has a present unconditional obligation at the reporting date, and therefore would have a liability, if it violates a requirement or another obligating event has occurred.

In addition, the Board tentatively decided that an entity has a present unconditional obligation that has an associated conditional obligation (stand ready obligation) when:

- a statute requires the entity to provide risk protection
- an entity separately agrees to bear another's risk that arises from being subject to the statute.

However, the Board tentatively decided that an entity would not recognise a liability, or essentially does *not* have a present unconditional obligation:

- to comply with statutes not yet effective

- for expected future actions or intentions
- to transfer economic resources to comply with the law; an obligating event also must have occurred.

Dealing with Uncertainties

The Board tentatively decided that the definition of a liability should be applied to assess whether a liability exists at the reporting date, and if a liability exists at that time, then uncertainly regarding the amount would be considered in measuring the liability. The Board also determined that this approach could be applied to any element of the financial reports in which uncertainties exist.

In addition, the Board discussed possible revisions to the working definition of a liability to state that an economic obligation:

- must be unconditional
- is something that is capable of resulting in "provision of an economic resource"

Extractive Activities Research Project

The Board discussed the findings of the extractive activities research project team, specifically in regards to the initial recognition of minerals and oil and gas reserves and resources.

The project team presented the types of assets that would be recognised throughout an extractive activities operation. The timing of recognition for these assets would depend on the stage of the upstream activities (i.e., exploration through to extraction).

In addition, the project team recommended limiting the geographical size of the unit of account for assets, e.g., to the field or mine level, and that it would depend on whether the entity was in the exploration, development or extraction phase of an operation.

Overall the Board agreed with the recommendations of the project team. The Board instructed the project team to propose for a future meeting:

- disclosure issues
- the outline of the proposed discussion paper.

The discussion paper is expected to be published in the fourth quarter of 2008.

Fair Value Measurement Project

The Board deliberated the scope of the fair value measurement project and reaffirmed its preliminary views on the attributes specific to an asset or liability, whether transaction costs are separate from fair value and the fair value hierarchy, as documented in Discussion Paper (DP) *Fair Value Measurements*.

Financial Statement Presentation

The Board continued discussing the financial statement presentation project and decided that the DP would not address:

- changes to the presentation of items currently included in other comprehensive income (OCI)
- "recycling" practices
- capital management disclosures
- measurement uncertainty disclosures
- earnings per share presentation
- additional segment disclosures.

However, the Board decided to propose, for the DP, that an entity should present:

- a single statement of comprehensive income
- items of OCI in a separate section according to the category (operating, investing or financing) to which it relates
- income tax assets, liabilities and cash flows separately in the statements of financial position and cash flows.

In addition, the Board decided that the DP would include the view that income taxes should be allocated between continuing and discontinued operations, items of OCI, and items recognised directly in equity.

The Board also noted that the schedule reconciling the statement of cash flows to the statement of comprehensive income would:

- not include equity transactions
- include changes in assets and liabilities, other than for remeasurements, in a single column.

Lastly, while not included in the proposals for the DP, the Board decided the related ED would address offsetting and disclosures about the measurement bases of assets and liabilities.

A DP is expected to be published in September 2008 with a six-month comment period.

Hedge Accounting

The Board had previously confirmed that the scope of the amendments to IAS 39 *Exposures Qualifying for Hedge Accounting* would be limited to:

- designating a purchased option in its entirety as a hedging instrument of an item containing no optionality in a manner that would result in zero ineffectiveness
- hedging inflation risk in certain situation.

The Board confirmed that the amendments would be applied retrospectively and tentatively decided that they would be effective for annual periods beginning on or after 1 July 2009.

In addition, the Board held an education session on the U.S. Financial Accounting Standard Board's (FASB)

project on hedge accounting, discussing the proposals in the recently published FASB ED on *Accounting for Hedging Activities*. No decisions were made.

Small and Medium-sized Entities

The Board continued its redeliberations of the proposals contained in the ED of an *IFRS for Small and Medium-sized Entities* (to be changed to *IFRS for Private Entities*), and specifically discussed issues related to the ED Sections 4-12.

Presentation of Financial Statements

The following tentative decisions were made by the Board:

- The statement of financial position would be based on liquidity if this provides reliable and more relevant information than a current / non-current classification.
- Expenses may be presented either by nature or by function of expense. If by function, further disclosures would not be required.
- The presentation of a combined statement of comprehensive income and retained earnings may be permitted in certain circumstances in place of separate statements of comprehensive income and changes in equity.
- A statement of cash flows would be required, using either the direct or indirect method.

Consolidated, Separate and Combined Financial Statements

Consolidated financial statements would be required for private entities that are parent entities, and there would be no temporary control exemption.

Separate financial statements would not be required; if prepared, an entity could elect cost or fair value through profit or loss for each category of investment.

The description of combined financial statements, as currently drafted, would

be retained, with further guidance to be added.

Accounting Policy Hierarchy

The accounting policy hierarchy will be modified to remove the:

- requirement for management to consider guidance in full IFRSs
- reference to recent pronouncements of other standard setters, other literature and industry practice.

Inventories

The Board did not have any changes to the proposed principles on inventories contained in the ED.

Financial Instruments

In regards to Section 11 of the ED *Financial Assets and Financial Liabilities*, the Board decided to amend the section to:

- explain how to apply it to simple financial instruments
- clarify, with examples, that the cost model typically will be applicable to the majority of financial instruments held by private entities
- simplify the guidance on fair value measurement principles
- maintain the effective interest rate method and to not allow straight-line amortisation of premiums and discounts
- add guidance clarifying the types of risks eligible for hedge accounting, but not allow the use of debt instruments as hedging instruments
- include guidance on measuring hedge effectiveness, but not permit the use of the short-cut method
- add guidance on accounting for factoring transactions
- tentatively remove the option to follow the accounting for financial instruments under full IFRSs in place of Section 11
- state that an impairment loss for an equity instrument recognised at cost would be the difference

between its carrying amount and the best estimate of the amount to be received if the asset were sold

- clarify that an interest rate swap would be measured at fair value through profit or loss.

IFRIC Update

It was noted that the IFRIC had completed its redeliberations on D21 *Real Estate Sales* and D22 *Hedges of a Net Investment in a Foreign Operation* and both interpretations were approved by the Board.

Valuation Expert Advisory Panel

The Board reviewed the findings from the first meeting of the valuation expert advisory panel (the advisory panel). The advisory panel identified a variety of measurement issues that it should address, including:

- the use of valuation techniques and calibration of, and adjustment to, valuation models
- the use of third-party price quotes

- the determination of what constitutes active from inactive markets
- the use of the fair value hierarchy for disclosure purposes
- the disclosure of sensitivities and ranges.

The advisory panel plans to first address valuation practice issues and then the related disclosure issues.

Technical Plan

The Board discussed its updated technical plan and project timetables, which are available on the IASB Web site.

IASB Observer Notes

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