

CONCLUSIONS ON IFRIC REJECTION NOTES

Summary Note of Meeting 27 November 2006
between delegations from CESR, BUSINESSEUROPE¹ and FEE/Audit Firms

25 January 2007

On 27 November a meeting took place between delegations from CESR, BUSINESSEUROPE and the accountancy profession (appendix 1) to discuss the implications of IFRIC rejection notes for financial reporting in Europe and the necessary enhancement of the due process around IFRIC rejection notes. In this meeting a number of conclusions were reached, which are set out in the summary note below. The meeting was informal in nature but each of the organisations has subsequently indicated their support for conclusions reached in part I.

Issue

The issue is whether or not the IFRIC rejection note itself or the explanatory text included in an IFRIC rejection note, should result in an accounting change and, if so, whether the change should be regarded as the correction of an error or a change in accounting policy. The accounting treatment of restatement is the same under IAS 8 (based on IAS 8.5 and as set out in respectively IAS 8.14 (changes in accounting policy) and IAS 8.42 (correction of an error)), but the legal consequences might be different depending on the regulatory environment.

Issues reach IFRIC generally because there are various possible understandings of IFRS requirements or there is a conflict of views. Some argue that many such conflicts are transitional issues and will disappear over time as all stakeholders become more familiar with the interpretation and application of IFRS. It is also said that the existence of these possible understandings is unavoidable within a set of principles-based standards. The IFRIC rejection notes – although not officially part of IFRS – are likely to have a significant effect on the consistent application of IFRS. However, some stakeholders have questioned whether a rejection note should be considered to be part of IFRS guidance, as rejections do not follow the same due process as “real” interpretations. Some parties (including auditors, market regulators and some issuers) consider that, even if rejections are not officially IFRS guidance, they help to clarify the meaning of part of a standard or the way certain provisions need to be interpreted or applied, in the same way as illustrative examples and application guidance that are appended to accounting standards. As such, they assist users in forming their judgement. Others question if rejection notes are necessary.

¹ On 24 January UNICE changed its name to BUSINESSEUROPE.

Rejection notes on items not added to the IFRIC agenda are not part of IFRSs. Consequently, they are not endorsed by the European Commission. In that sense they have no official status within Europe. They are also not examined by EFRAG.

Rejection notes that include an explanation represent a clarification of the standard concerned and, even though not officially part of IFRS, form an important source of guidance. Therefore, rejection notes need to be subject to a sufficiently robust due process.

I: Implications of IFRIC Rejection Notes

There was broad agreement among the participants in the meeting on the following:

- The objective of all changes that would result from the items set out below would be to provide clear and unambiguous information to the markets. As expertise in the application of IFRSs will develop over time the approach described below could be considered transitional and may need to be re-visited in due course for example when IFRIC's new due process has proved to be effective.
- IFRIC rejection notes representing clarifications of standards, though not officially part of IFRS, form an important source of guidance, especially during the current transitional period in which all stakeholders are learning about the application and interpretation of IFRS.
- In view of the principles-based nature of IFRS, consistent application does not always mean identical application. Rather consistent application means that the application is acceptable by reference to the standards and is therefore within the boundaries of IFRS. This means that also depending on the circumstances of the individual company there can be more than one approach that can be followed, thereby leading to variances in practice.
- If the IFRIC considers whether or not it should add a particular issue to its agenda, this means that in almost all circumstances the issue is a genuine one about which there is doubt as to the appropriate accounting treatment. The working assumption would be that an accounting policy applied in the previous financial statements prior to an IFRIC rejection note was based on a reasonable interpretation of the relevant standard at the time the accounting policy was selected considering the available IFRS guidance at that time.
- As IFRIC rejection notes often provide clarification of the standards, there is an expectation on the part of stakeholders in IFRS that IFRIC rejection notes will be carefully considered by preparers in determining their accounting policies. In the case of a change in a previous accounting treatment following the issue of an IFRIC rejection note, a company should apply IAS 8 and provide proper and sufficient disclosure of the reasons for the change, having regard to the particular facts and

circumstances of the individual case, including reference to the IFRIC rejection note. While the issue description above distinguishes between a change in accounting policy and the correction of an error, the conclusion at least for a transitional period was that, in most cases and with appropriate note disclosure, it would not be necessary to be explicit in the disclosure and only the facts should be represented. Wording on the change in accounting treatment could be along the following lines: “The company previously accounted for [explanation of previous accounting practice]. Following the publication in the [date] IFRIC Update of the IFRIC agenda decision on [item X] the company has reconsidered its accounting treatment applied to those transactions and decided to adopt the treatment set out in the IFRIC agenda decision. Accordingly [description of the new treatment]. This change in accounting treatment has been accounted retrospectively, and the comparative statements for 200X have been restated. The net effect (increase/decrease) on retained earnings as of that date amounts to [amount]”.

- When a company decides to continue applying an accounting policy that appears to be inconsistent with an IFRIC rejection note, the burden of proof is on the company to explain why the accounting policy concerned is nevertheless appropriate.

II: Enhancement of due process around IFRIC rejection notes

There was broad agreement among the participants in the meeting on the need for the following enhancements in the due process relating to IFRIC rejection notes:

- Status of a rejection note:
 - Rejection notes cannot have the same status as interpretations, but it needs to be clarified what status they have. Rejection notes should have the status of implementation guidance since they have the same objective as implementation guidance, and be subject to the IASB quality criteria.
 - Rejection notes should be considered when standards are reviewed and withdrawn when superseded by changes in standards or other guidance.
- Transparency:
 - Agenda committee: improved transparency and communication is needed. This can be achieved in different ways. One way would be to publish detailed minutes of meetings of the committee, including descriptions of all the issues reviewed by the committee. Alternatively, consideration might be given to making agenda committee meetings public meetings. The composition of the agenda committee should be well balanced.
 - Rejection notes: final rejection notes should explain how IFRIC has addressed any significant issues and new arguments that were raised in comment letters on tentative agenda decisions.

- Voting: Simple majority voting is not sufficient for rejection notes. The voting process should be at least the same as for draft interpretations: i.e. qualified majority.
- Involvement IASB: The Board should not participate directly in the IFRIC rejection note process. However, the Board should notify IFRIC in case of its disagreement with tentative IFRIC agenda decisions, and the Board should be consulted when there is a large number of comment letters or when stakeholders substantially disagree on tentative IFRIC agenda decisions.
- Comment period: A comment period of 30 days for draft rejection notes is very short, although it is recognised that the period needs to be kept short in order not to slow the process unduly, and it is suggested that the period should be extended to 45 days.

Present at the meeting of 27 November 2006:

CESR:

Paul Koster, Chairman CESRFin
Sophie Baranger
Javier Ruiz del Pozo, CESR Secretariat
Marion Bougel-Bomtemps, CESR Secretariat

BUSINESSEUROPE:

Peter Sampers, Deputy Chairman Accounting Harmonisation Group
Françoise Flores (by phone)
Bernd Hacker

Profession* :

Hans van Damme, FEE Vice-President
Mireille Berthelot, Deloitte
Andrew Buchanan, BDO
David Lindsell, Ernst & Young
Saskia Slomp, FEE Secretariat
Catherine Ameye, FEE Secretariat

* Representatives from BDO, Deloitte and Ernst & Young were present at the meeting, representing the FEE EC Roundtable Group in which BDO, Deloitte, Ernst & Young, Grant Thornton, KPMG, Mazars and PwC participate.