

## Welcome to IASB Update

This IASB Update is a staff summary of the tentative decisions reached by the Board at a public meeting. As a project progresses, the Board can, and sometimes does, modify its earlier tentative decisions. Tentative decisions do not change existing requirements until those decisions are incorporated in a new or amended standard.

The IASB met on 11 and 12 May 2011 in a public meeting, with some Board members participating by telephone or videoconference. The meeting was held jointly with the FASB with FASB Board members participating via videoconference from Norwalk.

The topics discussed at the joint IASB/FASB meeting were

- Revenue recognition: education session
- Insurance contracts

The topics discussed at the IASB meeting were

- Leases: education session
- Insurance contracts
- IFRS 9: Financial instruments—hedge accounting

## IASB / FASB sessions

### Revenue recognition: education session

The IASB and FASB invited guest speakers from the telecommunications industry to present their views on how the proposed revenue recognition model would affect current accounting practice in the industry.

The external presenters were Thilo Kusch and Heiko Ehrcke of the Deutsche Telekom group, representing a forum of European telcos; Goran Nilsson and Kristinia Beckius from TeliaSonera AB; and Ryan Siurek and John Mutrie from Sprint Nextel Corp, representing a US telcos forum. Because this was an education session the boards were not asked to make any decisions.

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#### Future Board meetings

The IASB meets at least once a month for up to five days.

The next Board meetings in 2011 are:

16-20 May  
31 May and 1 June  
13-17 June

To see all Board meetings for 2011, [click here](#).

#### Archive of IASB Update Newsletter

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#### Podcast summaries

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## Insurance contracts

### Measurement of policyholder participation

The boards considered how to apply the principle that an insurance contract is measured using the expected present value of the fulfilment cash flows when those cash flows result from contractual participation features.

The IASB made the following tentative decisions.

- a. The measurement of the fulfilment cash flows relating to the policyholder's participation should be based on the measurement in the IFRS financial statements of the underlying items in which the policyholder participates. Such items could be assets and liabilities, the performance of an underlying pool of insurance contracts or the performance of the entity. The staff will consider whether this approach creates a need for any specific disclosures.
- b. An insurer should reflect, using a current measurement basis, any asymmetric risk-sharing between insurer and policyholder in the contractually linked items arising from a minimum guarantee.
- c. An insurer should present changes in the insurance contract liability in the statement of comprehensive income consistently with the presentation of changes in the linked items (ie in profit or loss, or in other comprehensive income).
- d. The same measurement approach should apply to both unit-linked and participating contracts.

The IASB will consider related disclosures at a future meeting.

Nine members of the IASB voted in favour of this decision, four voted against and one abstained. One IASB member was not present. In addition, the IASB tentatively decided to proceed with the proposals in the IASB's exposure draft (ED) for consequential amendments relating to the following items held in unit-linked funds: financial instruments issued by the insurer (eg treasury shares) and owner-occupied property. The majority of the IASB members present supported the decision (one voted against).

The FASB tentatively decided that the measurement of the liability should reflect the expected present value of the cash flows, discounted at current rates, using the contractual measurement basis for the underlying items in which the policyholder participates. The majority of FASB members supported this decision. The FASB plans to consider at a future date whether to address accounting mismatches through the measurement of the items that a policyholder participates in.

## IASB sessions

### Leases: education session

The IASB discussed the following topics in an education session in anticipation of the joint meeting with the FASB in the week beginning 16 May:

- Shariah-compliant leases—lessor issues
- Contract modifications or changes in circumstances after the date of inception of the lease
- Distinguishing between lease accounting approaches
- Lessee accounting—other-than-finance lease

- Lessor accounting: finance leases—measurement and presentation
- Lessor accounting other-than-finance leases
- Reassessment of options in a lease
- Reassessment of the discount rate in a lease.

The Board was not asked to make any decisions.

## Insurance contracts

The IASB continued its discussion on insurance contracts by considering whether to present in other comprehensive income changes in the carrying amount of insurance contract liabilities arising from the difference between the current discount rate and the discount rate at inception. The discussion was not held jointly with the FASB because of differences in underlying financial statement presentation between IFRSs and US GAAP and in the presentation requirements for gains and losses on the assets backing insurance contracts.

The Board was not asked to make any decisions.

### Assets backing insurance liabilities

The Board tentatively decided not to change the requirements for presenting gains and losses on assets held to back insurance contract liabilities. In making its decision the Board noted that this was on the assumption that changes in the carrying amount of the insurance contract liability are not presented in other comprehensive income. If that were to change, the treatment of assets backing insurance contract liabilities might need to be revisited. All IASB members present supported this decision.

### Next steps

Both boards will continue their discussion on this project at their joint meeting on 17-19 May 2011.

## IFRS 9: Financial instruments—hedge accounting

At this meeting the IASB continued its redeliberations on the exposure draft (ED) *Hedge Accounting* and discussed the proposed hedge effectiveness assessment (to qualify for hedge accounting). The Board discussed:

- clarification of the requirement of achieving 'other than accidental offsetting'; and
- the meaning of the requirement that a hedging relationship should produce an 'unbiased' result and minimise expected hedge ineffectiveness.

### Clarification of the term 'other than accidental offsetting'

Feedback from comment letters and from the outreach activities showed strong support for moving from a quantitative threshold-based assessment to a principle-based assessment. The feedback also highlighted a request for further guidance on the meaning of the term 'other than accidental offsetting'.

The Board considered that the feedback showed that the use of umbrella terms such as 'other than accidental offsetting' that comprise several aspects was abstract, which made them difficult to understand.

The Board noted that the criterion of 'other than accidental offsetting' was intended to comprise two aspects:

- a. the notion of an economic relationship between the hedged item and the hedging instrument, which gives rise to offset; and
- b. the effect of credit risk on the level of offsetting gains or losses on the hedging instrument and the hedged item, which may reduce or modify the extent of offsetting.

The Board tentatively decided to disaggregate the umbrella term 'other than accidental offsetting' and instead to directly refer to those two aspects and add some application guidance.

All Board members supported this decision.

Meaning of the requirement that a hedging relationship should produce an 'unbiased' result and minimise expected hedge ineffectiveness

Feedback from comment letters and from the outreach activities showed that while there was strong support for the overall move to a more principle-based assessment, there was uncertainty about how the different elements of the proposal relate to each other and about their meaning as well as concern about some of their implications. There was a general request for greater clarification.

The Board discussed the four elements of the objective of the hedge effectiveness assessment that were proposed in the ED:

- that the hedging relationship will produce an 'unbiased' result;
- that the hedging relationship will minimise expected hedge ineffectiveness;
- that the entity has no expectations that the changes in the fair value of the hedging instrument will systematically either exceed or be less than the changes in the fair value of the hedged item such that it will produce a biased result; and
- that the hedging relationship shall not reflect a deliberate mismatch between the weightings of the hedged item and the hedging instrument that would create hedge ineffectiveness.

The Board noted that the reference to an 'unbiased' result was confusing and, as it is worded now, the proposals could be perceived as requiring entities to identify the 'perfect' hedging instrument as a starting point for hedge accounting instead of the instrument that is actually being used as the hedge. The Board also noted that referring to the term 'unbiased' creates the issue of referring to 'umbrella' terms that introduce abstraction and make the requirements less understandable.

The Board also noted the proposed requirement that the entity should have no expectations that the changes in the fair value of the hedging instrument will systematically either exceed or be less than the changes in the fair value of the hedged item can create a problem because the fair value of the hedging instrument at the time of designation is a present value. Hence, in situations in which a derivative is in- or out-of-the-money when designated as the hedging instrument there is an effect from the present value at that point that will accrete to the undiscounted amount (this is known as unwinding of the discount). As a result there would be an expectation that the changes in the value of the hedging instrument would systematically exceed or be less than those of the hedged item. The Board considered that this was neither intended nor useful.

As a result of its discussion of the elements the Board tentatively decided to remove the references to the umbrella term 'unbiased' and 'minimising expected hedge ineffectiveness' and the requirement that an entity should have no expectation that the changes in the value of the hedging instrument will systematically either exceed or be less than the change in value of the hedged item.

Instead the Board tentatively decided to proceed with an approach that refers more directly to the

following:

1. That an entity's designation of the hedging relationship shall be based on the 'economic hedge' ie:
  - a. the quantity of hedged item that it actually hedges; and
  - b. the quantity of the hedging instrument that it actually uses to hedge that quantity of hedged item.
2. However, the Board also tentatively decided that an entity shall not designate a hedging relationship such that it reflects an imbalance between the weightings of the hedged item and hedging instrument that would create hedge ineffectiveness (irrespective of whether recognised or not) in order to achieve an accounting outcome that is inconsistent with the purpose of hedge accounting. (Such an outcome might, for example, be intended to avoid recognising hedge ineffectiveness for cash flow hedges or to achieve fair value hedge adjustments for more hedged items with the aim of increasing the use of fair value accounting, but without offsetting fair value changes of the hedging instrument.)

All Board members supported this decision.

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