



## EFRAG TEG **UPDATE** JULY 2007

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### Summary of the EFRAG CFSS and TEG meetings in July 2007

On Wednesday 11 July 2007 EFRAG TEG (EFRAG) met with the national standard-setters of Europe in EFRAG's Consultative Forum of Standard-Setters (CFSS) to discuss:

- The joint IASB/FASB project on Financial Statement Presentation
- The PAAinE paper on Stewardship
- The IASB ED of a proposed IFRS for SMEs

On Thursday 12 and Friday 13 July 2007 EFRAG held its monthly meeting and discussed:

- IFRIC 13 *Customer Loyalty Programmes*
  - The IASB's *Insurance Contracts* Discussion Paper
  - Amendment to IFRS 2 *Share-based Payment: Vesting Conditions and Cancellations*
  - IAS 1 (Revised) *Presentation of Financial Statements*
  - The IASB project on Business Combinations
  - IFRIC D21 *Real Estate Sales*
  - The IASB's Annual Improvements Project
  - IFRIC 14 IAS 19 *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*
  - The IASB's Joint Ventures project
  - The IASB's ED of a proposed IFRS for SMEs
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### EFRAG CFSS meeting on 11 July 2007

At their July meeting, EFRAG and Europe's national standard-setters were updated on **the joint IASB/FASB project on Financial Statement Presentation**. Participants heard that the objective of the project is to develop a common, high-quality standard for presentation of information in the financial statements, including the classification and display of line items and the aggregation of line items into subtotals and totals. The Boards have adopted the working principle that financial statements should present information in a manner that:

- portrays a cohesive financial picture of an entity;
- separates an entity's financing activities from its business and other activities and further separates financing activities between transactions with owners in their capacity as owners and all other financing activities;
- disaggregates line items if that disaggregation enhances the usefulness of that information in predicting future cash flows;
- helps users to assess the reporting entity's ability:
  - to meet its financial commitments as they come due and to invest in business opportunities; and
  - to generate future cash inflows, the difference between cash transactions and accrual accounting, and the effects of noncash activities during the period on the entity's financial position; and
- helps users to understand the basis on which assets and liabilities are measured and the uncertainty inherent in and sensitivity of those measures.

Participants also heard that decisions had not yet been taken on whether the standard being developed would allow or require an 'Other Comprehensive Income' category, whether recycling would be prohibited, and what totals and sub-totals would be allowed or required.

The IASB's current timetable envisages a discussion paper being issued around the end of 2007, and EFRAG will continue to monitor the project closely.

Participants also received a presentation based on the recently-issued **PAAinE** (Proactive Accounting Activities in Europe) **paper on Stewardship**. The IASB and FASB proposed, in a discussion paper issued in 2006, that the only objective of financial statements should be to provide information that is useful for making resource allocation decisions (the resource allocation decision usefulness objective). Many of those responding to the IASB/FASB paper disagreed with the Boards' views on stewardship and the objective of the PAAinE paper had been to help the Boards by identifying the common themes in the comment letters on stewardship, discussing the meaning of stewardship and considering what the implications might be of a separate stewardship objective. The main conclusions of the paper were that:

- the stewardship objective (also known by some as the 'accountability objective') focuses on both past performance and how the entity is positioned for the future. As such, it is broader than the resource allocation decision usefulness objective described in the IASB/FASB paper; and
- the majority of respondents to the discussion paper believe that financial statements should continue to have a stewardship objective.

The IASB and FASB are currently discussing the comments received in response to their discussion paper, and the current intention is to issue an exposure draft based on the discussion paper later this year.

The PAAinE paper on Stewardship is available from EFRAG's website ([www.efrag.org](http://www.efrag.org)).

EFRAG and the European national standard-setters also discussed the field-testing that the IASB is planning to carry out of its **ED of a proposed IFRS for SMEs.**, and other activities the standard-setters are carrying out relating to the ED. The standard-setters also had an initial discussion of EFRAG's draft comment letter on the ED. That draft letter is available from EFRAG's website ([www.efrag.org](http://www.efrag.org)). Comments are invited by 31 August 2007.

#### **EFRAG TEG meeting on 12 and 13 July 2007**

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At its July meeting, EFRAG discussed **IFRIC 13 Customer Loyalty Programmes** in order to start developing EFRAG's draft endorsement advice on the interpretation.

Some entities grant 'points', air miles or other award credits to their customers as part of a sales transaction with those customers, and IFRIC 13 explains how existing standards should be applied to such transactions. It requires:

- the transactions to be treated as comprising two elements—the basic sale transaction and the sale of rights in respect of a future transaction;
- the fair value of the total consideration received to be allocated between the two elements by reference to their fair value; and
- recognition in the income statement of the consideration allocated to the grant of award credits to be deferred until, usually, the award credits are redeemed.

Although EFRAG members raised some concerns about the interpretation, they agreed that EFRAG's draft letter should recommend endorsement. EFRAG's draft endorsement advice letter is now being prepared, and it is expected that it will be issued in September.

In June, EFRAG held a special one-day meeting to discuss the **IASB's Insurance Contracts Discussion Paper** and to develop views for inclusion in EFRAG's draft comment letter on the paper. That discussion continued at the July meeting, where the focus was on liability recognition and measurement; in particular on the rationale for and appropriateness of the proposals on risk margins, service margins, and non-entity specific measures. EFRAG members discussed the proposals both as they applied to insurance liabilities and also as they might apply to other types of liabilities. No final decisions were taken and EFRAG's discussion will continue. The current intention is to issue EFRAG's draft letter for comment by the end of September.

EFRAG also continued its discussions on the draft endorsement advice it should give on the not-yet-issued standard, the **Amendment to IFRS 2 Share-based Payment: Vesting Conditions and Cancellations**. Although some EFRAG members had concerns about aspects of the Amendment, EFRAG's tentative view was that, subject to changes made by the IASB in finalising the Amendment, EFRAG's draft endorsement advice letter should recommend endorsement. EFRAG will finalise its draft advice when the Amendment has been issued.

Back in April, EFRAG considered a near-final draft of **IAS 1 (Revised) Presentation of Financial Statements** and started to develop its draft endorsement advice on the revised standard. EFRAG continued those discussions at its May and July meetings.

Although IAS 1 Revised has not yet been issued, it is expected to require:

- changes in net assets that have not arisen as a result of transactions with owners as owners (so-called non-owner changes in equity) to be shown in either one or two statements of comprehensive income, and no owner changes in equity can be included in that statement or those statements.
- the effects of recycling to be disclosed.
- the income tax relating to each component of other comprehensive income to be disclosed separately.
- a balance sheet showing the position at the beginning of the corresponding period to be presented if there has been a prior year adjustment.
- dividends to be disclosed either on the face of the statement of changes in equity or in the notes, but not in the statement(s) of comprehensive income.

The names of the primary financial statements will also be changed, although entities will not be required to use the new names in their published financial reports.

EFRAG has tentatively decided to recommend endorsement of IAS 1 Revised and a draft endorsement advice letter will be issued for comment—and made available on EFRAG's website ([www.efrag.org](http://www.efrag.org))—when IAS 1 Revised has been issued.

Over the last few months EFRAG has been discussing various aspects of the **IASB project on Business Combinations** in order to develop its thoughts on the draft endorsement advice it might give when IFRS 3 (Revised) *Business Combinations* and IAS 27 (Revised) *Consolidated and Separate Financial Statements* are issued. It is already clear from these discussions that a number of EFRAG members have fundamental concerns about the revised standards.

In July EFRAG discussed four more issues addressed in the revised standards—transactions with non-controlling interest (NCI) holders that do not result in a loss of control, contingent consideration, acquisition-related costs and bargain purchases—and various further concerns were raised. EFRAG's discussion of its draft endorsement advice on the revised IFRS 3 and IAS 27 will continue in the autumn.

EFRAG also discussed **IFRIC D21 Real Estate Sales** with a view to developing a draft comment letter. D21 seeks to provide guidance on the type of real estate transactions that fall within the scope of IAS 11 *Construction Contracts* as opposed to IAS 18 *Revenue*. It argues that IAS 11 applies only to contracts for construction services, and it sets out some indicators that it proposes should be used to determine whether a real estate contract is a contract for construction services. EFRAG members generally were not very comfortable with the proposals in D21 and they raised a number of fundamental concerns. A draft comment letter will now be prepared. It is expected that the draft letter will be issued for comment in September.

Changes to IFRS, however small, are time-consuming and burdensome for all those with an interest in the standard-setting process. With the intention of easing the burden for all concerned, the IASB has developed a process for dealing with non-urgent, minor amendments to IFRS (termed the 'annual improvements process'). This process involves the IASB discussing proposals for non-urgent, minor amendments to standards throughout the year and then, once a year, issuing a combined ED (and eventually a combined IFRS implementing the changes). The first ED in **the IASB's Annual Improvements Project** is expected to be issued in early October. At its July meeting EFRAG discussed eleven of the three dozen or so proposed amendments that will appear in the final ED. The purpose of the discussion was to enable staff to start developing an initial draft of EFRAG's comment letter.

EFRAG's discussion of this project will continue in the autumn.

Earlier this month IFRIC issued **IFRIC 14 IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction**. At its July meeting EFRAG discussed the draft endorsement advice it should issue in respect of the interpretation. EFRAG members were generally comfortable with the interpretation and asked staff to prepare a draft letter recommending endorsement. That draft letter has since been approved and issued for comment, and is available from EFRAG's website ([www.efrag.org](http://www.efrag.org)).

EFRAG also discussed the latest thinking in **the IASB's Joint Ventures project**. The principal proposal seems likely to be that IAS 31 *Interests in Joint Ventures* should be amended to eliminate proportional consolidation as one of the acceptable accounting methods for jointly-controlled entities. This would have the effect of substantially reducing the difference between IFRS and US GAAP in this area, whilst also eliminating an inconsistency between IFRS and the existing Framework. The other main proposal is likely to be that the material in IAS 31 on the different types of joint arrangement—joint operations, joint assets and joint ventures—will be clarified and improved.

The main concern of EFRAG members was whether the effect of these proposals would be a loss of accounting information. Some suggested that proportional consolidation provides users with information they find useful, and the new disclosure requirements that the IASB is expected to propose would provide less information. On the other hand, some others suggested that the proposed clarifications of 'joint operations' and 'joint assets' might result in more joint arrangements being treated as joint operations or joint assets rather than joint ventures, which could mean that in practice there would not be a loss of information.

After discussion it was agreed that EFRAG should set up a Joint Ventures Working Group to help it assess the implications in practice of the proposals. A public call for nominations for the Working Group has now been posted on EFRAG's website ([www.efrag.org](http://www.efrag.org)). The deadline for nominations is 24 August.

EFRAG will discuss the project further at a future meeting.

EFRAG issued its draft comment letter on **the IASB's ED of a proposed IFRS for SMEs** in April. However, that draft letter did not contain any comment on the ED's disclosure proposals (because EFRAG decided to defer its consideration of those proposals so that it could issue the draft letter earlier). At its July meeting it discussed the disclosure proposals and concluded that they are too detailed and burdensome for both for preparers and for users. It was agreed that the draft comment letter should be amended to incorporate this view. The revised draft letter has now been issued and is available from EFRAG's website ([www.efrag.org](http://www.efrag.org)).

EFRAG will hold its next meeting in Brussels on **Wednesday 5 to Friday 7 September 2007**. On 5 September, EFRAG will also meet with the national standard-setters of Europe in the Consultative Forum of Standard-setters (CFSS).

EFRAG has recently issued, jointly with various European standard-setters, a PAAinE discussion paper entitled *Revenue Recognition: A European Contribution*. The paper was prepared jointly by staff of the German standard-setter and by EFRAG staff. Comments on the paper are invited by 10 December 2007. The paper can be downloaded from EFRAG's website ([www.efrag.org](http://www.efrag.org)).

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