

IFRS news

Emerging issues and practical guidance*

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The IASB's work programme and its implications

Leader of PwC's Accounting Consulting Services in the UK, Peter Holgate, looks at the IASB and FASB's updated convergence agenda published last month and asks, 'What's the rush?'

A major global event such as the Olympics has a clear, hard deadline for those running the show. Half-finished stadiums and building-site debris equals public embarrassment and global failure. Deadlines in standard-setting, however, ought to have a little more flexibility. Rushing to complete the IASB and FASB's convergence projects before Sir David Tweedie's retirement and publishing poorly thought-out standards would overshadow the great things he has achieved in his years as IASB chairman.

The IASB is in a difficult situation. A long and ambitious list of major projects are planned to be completed by June 2011 (see timetable p2), when Sir David and two other board members retire. This is also the deadline set by the Memorandum of Understanding, which outlines the joint work programme of the IASB and FASB. The SEC's decision on whether to introduce IFRS into the US is due in 2011 and is likely to be based on the MoU projects' completion.

Completion of this work programme in this timeframe and to the IASB's usual standard of quality is a significant challenge. It is not in anyone's interest for the IASB to rush to finalise its standards and compromise on quality in the process.

A high volume of new standards in a short timeframe will also be a considerable burden on entities (existing preparers and first-time adopters) and the investment community to: (a) absorb, consider and comment on the EDs; and (b) implement the new standards.

The boards' current position

The IASB and FASB issued a quarterly update last month, indicating that they are largely on target to complete the projects by June 2011. The IASB intends to issue exposure drafts in Q2 2010 that are 'significant both in nature and number ...eleven for the IASB (seven on major projects)'. The boards recognise that there are difficulties. Some of these are outlined below.

Financial instruments

The IASB and FASB 'have reached different conclusions on some technical issues', according to the first quarterly report. They add that 'addressing these differences in ways

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that foster convergence could affect the project timetables'. This seems to understate the situation. There are fundamental differences of views in the detail of this complex standard. It will be surprising if the boards can resolve these in order to finalise a standard in 14 months.

Insurance

The IASB and FASB again say that they 'have reached different conclusions on some technical issues' and that 'addressing these differences in ways that foster convergence could affect the project timetables described in this report'. Insurance accounting is also highly complex, and the publication of an ED has already been delayed a number of times. The boards' comments acknowledge that the timetable (ED in Q2 2010 and IFRS in Q2 2011) may not be realistic.

Lease accounting

An ED is imminent despite the boards agreeing in late March 2010 to explore an alternative approach to lessor accounting. The paper again acknowledges that 'that decision could affect the project timetables'. The focus has been mainly on lessee accounting; but to be worthwhile, the standard would need to deal with both lessee and lessor accounting. Again, a delay appears likely.

We encourage preparers to consider the boards' agendas and, if they are concerned about the burden on companies that these agendas represent, they should write to the boards. Concerns might include (a) the burden of considering and commenting on such a large batch of exposure drafts in the short term; (b) concerns about implementation of such a large amount of change.

IASB and FASB convergence timetable

Project	Expected publication date
IASB	
Consolidation: Disclosures about securitisation and investment vehicles	Final standard: June 2010
Financial instruments – liability classification and measurement	ED: May 2010 Final standard: Q4 2010 or Q1 2011
Financial instruments – hedge accounting	ED: June 2010 Final standard: Q4 2010 or Q1 2011
Joint arrangements	Final standard: June 2010
Post-employment benefits – defined benefit plans	ED: April 2010 (see this edition of <i>IFRS news</i> , p4) Final standard: Q1 2011
Derecognition	ED: TBC Final standard: TBC
Fair value measurement	ED: May 2010 Final standard: Q4 2010
FASB	
Financial instruments (comprehensive proposal)	ED: May 2010 Final standard: Q1 2011
Consolidation	ED: May 2010 Final standard: Q4 2010 or Q1 2011
Fair value measurement	ED: May 2010 Final standard: Q4 2010
IASB and FASB	
Financial statement presentation – organisation and presentation of information in the financial statements	EDs: May 2010 Final standard: Q1/2 2011
Financial statement presentation – presentation of items of other comprehensive income	EDs: May 2010 Final standards: Q1 2011
Financial statement presentation – discontinued operations	EDs: May 2010 Final standards: Q4 2010
Financial instruments with characteristics of equity	EDs: June 2010 Final standards: Q2 2011
Revenue recognition	EDs: May 2010 Final standards: Q2 2011
Leases	EDs: June 2010 Final standards: Q2 2011
Insurance contracts	EDs: June 2010 Final standards: Q2 2011

Cannon Street Press

Last round of 2008-10 'improvements' published

The Board has published 'Improvements to IFRSs' – a collection of amendments to seven IFRSs – as its latest set of annual improvements.

The Board uses the annual improvements process to make necessary, but non-urgent, amendments to IFRSs that will not be included as part of a major project. The latest batch of amendments (see below) includes those contained in the exposure draft, plus an amendment to IFRS 1, 'First-time adoption of International Financial Reporting Standards', which applies to entities with operations subject to rate regulation. That amendment was included in the exposure draft on rate-regulated activities, published in July 2009.

Amendments:

- IFRS 1, 'First-time adoption of International Financial Reporting Standards'
- IFRS 3, 'Business combinations'
- IFRS 7, 'Financial instruments: Disclosures'
- IAS 1, 'Presentation of financial statements'
- Transition requirements for amendments arising as a result of IAS 27, 'Consolidated and separate financial statements'
- IAS 34, 'Interim financial reporting'
- IFRIC 13, 'Customer loyalty programmes'

Unless otherwise specified, the amendments are effective for annual periods beginning on or after 1 January 2011, with earlier application permitted.

Extractive industries DP

The IASB published the extractive activities discussion paper last month. The working draft had been available on the IASB website, but the issuance of a formal DP and request for comment represents a major step by the Board. The DP responds to the many requests from the extractives industry for guidance on areas specific to them.

Highlights of the DP content include:

- Proposals for the definitions of reserves and resources, with PRMS and CRIRSCO templates suggested as preferred definitions.
- Asset recognition and measurement criteria, including the view that exploration and extraction rights form the basis of a recognisable minerals or oil and gas asset, with the unit of account relating to this contracting over time as exploration, evaluation and development activities take place.

- Historical cost being the measurement base of choice rather than fair value.
- Significant increases in the level of disclosure, with possible implications for management if regulators decide these disclosures should be audited.

Other areas of interest are not included within the paper, such as overlift/underlift, farm-outs and stripping costs. Some of these are being addressed through other projects.

The comment period ends 30 July 2010. The Board is expected to make a decision about adding the project to its agenda by the end of 2010; an exposure draft is likely to take at least 18 months following that decision. For more guidance on the requirements and impact, see the *IFRS news* supplement this month: 'Prospects for refined accounting'.

One in, one out at the IASB

Paul Pacter is to become a board member at the IASB with effect from 1 July 2010. He has elected to take on the membership of the Board for two years instead of the customary five. He has been director of small and medium-sized entities at the IASB for the last six years and will continue to chair the Board's new

SME implementation group. Paul fills the vacancy created by the retirement of Jim Leisenring at the end of June 2010. Jim has been a board member since January 2001. For a light-hearted review of Jim's tenure at the IASB, see next month's edition of *IFRS news*.

IFRIC appointments and reappointments

The IFRIC has announced that:

- Robert Garnett is to continue as chairman for two more years, despite retiring as a member of the IASB.
- Guido Fladt (PwC), Bernd Hacker (formerly of Siemens) and Andrew Vials (KPMG) have been reappointed for a further three-year term.
- Feilong Li, controller of CNOOC, China's largest producer of offshore crude oil and natural gas, has been appointed for a three-year term. He replaces Darrel Scott (FirstRand Banking Group), who has been appointed to serve as a member of the IASB from October 2010.



Significant changes ahead in accounting for employee benefits



The IASB has issued an exposure draft proposing significant changes to the recognition and measurement of employee benefit expense and to the related disclosure requirements. This amendment to IAS 19, 'Employee benefits', is the latest step in the project to revise IAS 19 following the discussion paper issued in 2008. The proposed amendments are not as far-reaching as the ideas in the discussion paper, but they will bring significant change. Tony Debell, partner in PwC's Global Accounting Consulting Services central team and 'Revenue, liabilities and other' topic team leader, and Richard Davis, director in ACS in the US, look at some of the detail.

The key proposals relate to:

- Recognition of actuarial gains and losses;
- Recognition of past-service cost;
- Measurement of pension expense;
- Presentation of pension expense; and
- Disclosure requirements.

More detail of the implications of the proposed changes is as follows:

- **Recognition of actuarial gains and losses:** actuarial gains and losses will be recognised immediately in 'other comprehensive income' (OCI). The 'corridor and spreading' option in IAS 19, which allows delayed recognition of actuarial gains and losses for post-employment benefits, will be prohibited. Immediate recognition in profit and loss, which is currently permitted for post-employment benefits and required for other long-term benefits, will also be prohibited. Actuarial gains and losses recognised in OCI will not be recycled through profit or loss in subsequent periods. Actuarial gains and losses arise both from changes in the assumptions used to measure pension and other long-term employee benefit obligations and from differences between previous assumptions and what has actually occurred in the period. These assumptions include, for example, assumptions about increases in salaries and pensions and the mortality rate, and the estimate of the discount rate. The proposed changes will mean increased balance sheet and total comprehensive income volatility for entities that currently use the corridor and spreading method.
- **Recognition of past-service cost:** all past-service cost will be recognised in profit or loss when the employee benefit plan is amended. Past-service cost arises when the terms of a benefit plan are amended to provide additional benefits for service the employee has already delivered. These additional benefits are sometimes conditional on the employee providing future service. IAS 19 currently requires past-service cost to be recognised on a straight-line basis until the future service has been delivered, or recognised immediately if no future service is required. This proposal means that past-service cost can no longer be spread over the future service period, which will increase volatility in profit or loss in the period in which plan amendments occur.

- **Measurement of pension expense:** the expected return on plan assets and the interest cost on the pension obligation will be replaced by a new method of calculating the finance cost associated with a funded pension obligation. The expected return on plan assets is the expected income from the assets held in a funded plan and the changes in the fair value of those assets. IAS 19 currently requires the expected return on plan assets to be one component of the annual cost of the plan, and the difference between this expected return and the actual return in the period is treated as an actuarial gain or loss.

The ED proposes that net interest expense or income will be calculated by applying an appropriate discount rate to the net surplus or deficit in the plan. The discount rate will be a high-quality corporate bond rate in markets where there is a deep market in such bonds, and a government bond rate in other markets. The measurement of interest cost for an unfunded plan remains unchanged.

The effect of this proposal is that the income earned on the assets held by a funded pension plan will be determined using the same discount rate that is used to calculate the present value of the pension obligation. The difference between this amount and the actual return in the period will continue to be treated as an actuarial gain or loss. The expected return on plan assets is usually higher than the discount rate, so the proposed change will increase the pension cost recognised in profit or loss for most entities with funded plans.

- **Presentation of pension expense:** IAS 19 will be amended to remove the flexibility around where in profit or loss the components of pension expense are recognised. The cost of benefits accrued in the current period (service cost) and benefit changes (past-service cost and curtailments) will be recognised as an operating expense. Interest expense or income will be recognised as a financing item. Any other re-measurements (actuarial gains and losses, the effects of the asset limitation and settlements) will be recognised net of tax in OCI.
- **Disclosure requirements:** additional disclosures will be required to present the characteristics of the entity's benefit

plans, the amounts recognised in the financial statements and the risks arising from defined benefit plans and multi-employer plans. The proposed changes will cover long-term benefits payable in service, as well as post-employment benefits, and are likely to increase the volume of disclosure for many entities.

The proposed changes will affect all entities that apply IAS 19 to defined benefit plans. They will:

- change the way that information about the benefit obligation is presented in the financial statements;
- increase the volatility in the post-employment benefit liability and in total comprehensive income for entities that currently use the corridor and spreading option for the recognition of actuarial gains and losses;

- increase the net pension cost for many funded pension plans; and
- change the line items in which employee benefit costs are reported for some entities.

These proposals could significantly change a number of performance indicators, including EBITDA, earnings per share and balance sheet ratios. Management should determine the effect of the proposed changes and how they should be communicated to shareholders and other users of the financial statements.

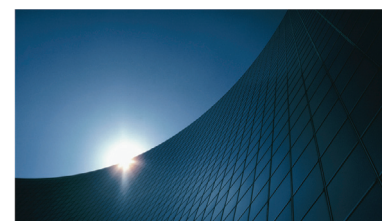
The comment deadline is 6 September 2010. A final standard is expected in 2011. The proposed changes are significant for entities with defined benefit plans; management should consider whether to comment on the proposals.

Interims: what should I do to prepare?

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