

AASB 29-30 May 2013 Agenda paper 11.10 (M131)



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Meetings

Accounting Standards Advisory Forum Meeting Summary—April 2013

23 April 2013

This is a summary of the meeting of the Accounting Standards Accounting Forum (ASAF) held in London on 8-9 April 2013. It was prepared by staff of the IASB, and is a high-level summary of the discussions that took place. A full recording of the meeting is available on the IASB website.

This was the inaugural meeting of the Accounting Standards Accounting Forum (ASAF) and it was held in London on 8-9 April 2013.

The meeting was chaired by Hans Hoogervorst, Chairman of the IASB, with Ian Mackintosh, Vice-Chairman of the IASB.

Related information

- Further information on the Accounting Standards Advisory Forum (ASAF)
- The Agenda Papers and recordings are available on the meeting page

ASAF Members attending

Kim Bromfield for the South African Financial Reporting Standards Council;
Alexsandro Broedel Lopes for the Group of Latin American Standard Setters;
Clement Chan for the Asian-Oceanian Standard-Setters Group;
Françoise Flores for the European Financial Reporting Advisory Group;
Gord Fowler for the Accounting Standards Board of Canada;
Liu Guangzhong for the Chinese Accounting Standards Committee;
Liesel Knorr for the Accounting Standards Committee of Germany;
Roger Marshall for the UK Financial Reporting Council;
Ana Martínez-Pina for the Instituto de Contabilidad y Auditoría de Cuentas (Spain);
Ikuo Nishikawa for the Accounting Standards Board of Japan;
Leslie Seidman for the Financial Accounting Standards Board (US); and
Kevin Stevenson for the Australian Accounting Standards Board.

Memorandum of Understanding

The meeting began with the signing of the Memorandum of Understanding (MoU) between the IFRS Foundation and the 12 members of the ASAF. A copy of the signed MoU can be accessed on the ASAF page of the IFRS Foundation website.¹

Conceptual Framework

IASB Members

The IASB members responsible for supporting this project participated in this session: Hans Hoogervorst, Ian Mackintosh, Stephen Cooper, Wei-Guo Zhang and Mary Toker.

Overview

The ASAF discussed the IASB's project to revise the Conceptual Framework. ASAF members had received copies of the papers on the Conceptual Framework that the IASB discussed at its February and March 2013 meetings. Taken together these papers comprise an initial draft of the Conceptual Framework discussion paper. ASAF members were asked to provide guidance on how to improve the arguments in the discussion paper and on any important areas or alternatives that might be missing. In particular, ASAF members were asked to provide comments on the following topics:

- a. Measurement;
- b. Presentation in the statement(s) of profit or loss and comprehensive income (including the question of what should be presented in other comprehensive income (OCI)); and
- c. Uncertainty, in the context of the definitions and recognition of assets and liabilities.

ASAF members also had a short discussion on the other topics to be included in the discussion paper.

Measurement (IASB February AP 3F Measurement principles, AP 3G Initial and subsequent measurement and March AP 5D Measurements other than cost or fair value)

Measurement principles

At the February 2013 meeting the IASB discussed the following measurement principles:

Principle 1: the objective of measurement is to represent faithfully the most relevant information about the economic resources of the reporting entity, the claims against the entity, and how efficiently the entity's management and governing board have discharged their responsibilities to use the entity's resources.

Principle 2: although measurement generally starts with an item in the statement of financial position, the relevance of information provided by a particular measurement method also depends on how it affects the statement of comprehensive income and if applicable, the statements of cash flows and of equity and the notes to the financial statements.

Principle 3: the cost of a particular measurement must be justified by the benefits of reporting that information to existing and potential investors, lenders, and other creditors.

ASAF members discussed these three principles and made the following comments:

- a. Some members supported the development of the three measurement principles. However, others stated that the proposed principles were just an extension of the qualitative characteristics of useful information and the objective of financial reporting. Consequently, they questioned whether they were needed.
- b. It was suggested that principle 1 should be split into two because there may be circumstances when the different objectives (information about resources and claims and information about how management has discharged its responsibilities) could result in different measurements.
- c. Some members were concerned about staff proposals to combine Principle 1 and Principle 2. They feared that this would place less emphasis on the objective of financial reporting when the IASB selects appropriate measurement bases.

- e. Some suggested that consideration of capital maintenance concepts might help with the development of the measurement principles.
- f. Some suggested that principle 3 was unnecessary as it was already included as an overarching consideration in the Conceptual Framework.

Initial and subsequent measurement

At the February 2013 meeting, the IASB tentatively decided that the most relevant measurement method will depend on:

- a. How the value of the asset will be realised.
- b. How the obligation will be fulfilled or settled.

ASAF members made the following comments on the proposed approach to initial and subsequent measurement:

- a. Some supported the proposed approach to deciding the most relevant measurement method for an asset or liability because it would reflect the way in which an entity manages its resources. However others disagreed with the approach stating that it would reduce comparability between entities.
- b. Some members suggested that the discussion of how an asset will be realised or an obligation fulfilled should be considered in the overall context of a business model approach to financial reporting.
- c. Some members stated that the discussion paper should discuss situations where there are significant differences between entry price and exit price.
- d. It was noted that the unit of account can affect measurement and it was suggested that the discussion paper consider the effect of the unit of account on measurement.
- e. Some members suggested that the discussion paper should discuss whether the measurement of assets and liabilities should reflect any linkage with other assets and liabilities.

Presentation of other comprehensive income (OCI, IASB March AP 5B Presentation in the Statement of Comprehensive Income – profit or loss and OCI)

At the March 2013 meeting, the IASB discussed the following three principles for determining whether a recognised item of income or expense should be presented in profit or loss or in OCI.

Principle 1: Items presented in profit or loss communicate the primary picture of an entity's financial performance for a reporting period.

Principle 2: All items of income and expense should be recognised in profit or loss unless presenting an item in OCI provides a better depiction of the financial performance.

Principle 3: An item that has previously been presented in OCI should be reclassified (recycled) to profit or loss if the reclassification results in relevant information about financial performance in that period.

ASAF members discussed these principles and how they could be used to identify two types of income or expense (bridging items and mismatched remeasurements) that would qualify for presentation in OCI. They made the following comments:

- a. Some suggested that the three principles could be used to identify types of income and expense other than the two types identified by the board that would qualify for presentation in profit or loss. For example, some suggested that the principles could be used to exclude from profit or loss highly volatile items that do not reflect the reporting entity's business model.
- b. It was suggested by some that defining profit or loss would provide a better basis for deciding what should be presented in OCI. Some stated that the discussion paper should describe what is meant by the terms financial performance, profit or loss and OCI.
- c. Some members expressed support for principle 3, which states that items should be recycled to profit or loss if reclassification results in relevant information about financial performance in that period. They noted that this approach was consistent with the view that profit or loss represents the primary picture of an entity's performance for a reporting period. Others opposed recycling, stating that permitting or requiring recycling was akin to allowing or requiring deferred income and deferred expenses.
- d. It was suggested by some that the proposed principles are simply an extension of the objective of financial reporting and the qualitative characteristics of useful information. Consequently, they questioned whether the principles would provide useful new guidance on what should be presented in profit or loss.
- e. Some suggested that the discussion on OCI should be linked more clearly with the measurement chapter. In particular, a decision to present in OCI should involve considering how cash flows arising from the asset or liability will be realised as well as an entity's business model, since these are also considerations in determining a measurement basis for the asset or liability.
- f. Some members stated that the IASB would need to clearly explain what it means by remeasurement. For example, is recognition of an impairment loss a remeasurement? They stated that if impairment was considered to be a remeasurement, then the principles could lead to impairment losses being recognised in OCI.
- g. Some suggested that rather than focusing on profit or loss and OCI, aggregation and presentation in the statement of comprehensive income should be based on how useful particular items of income and expense are in predicting future cash flows, with information that has similar predictive value grouped together.
- h. Some members noted that the asset revaluation model in IAS 16 Property, plant and equipment was inconsistent with the IASB's proposed approach to what should be presented in OCI. They recommended that the IASB consider this revaluation model as part of a separate project on capital maintenance and accounting for high inflation. Others suggested that capital maintenance issues should be dealt with in the Conceptual Framework rather than as part of a separate project.

Uncertainty, in the context of the definitions and recognition of assets and liabilities (IASB February AP 3B Elements – Definition of elements paragraph 14 and AP 3E Recognition and derecognition paragraph 24 – 34)

At the February 2013 IASB meeting, the IASB discussed removing the term 'expected' from the definition of an asset or liability. This would avoid implying that an item will not qualify as an asset or liability if the probability of an inflow or outflow does not reach some minimum threshold. In the IASB's view, as long as an item is capable of producing an inflow or outflow of resources, it can meet the definition of an asset or liability, even if the probability of an inflow or outflow is very low (eg out of the money options). Removing the reference to 'expected' flows from the definition would also remove confusion over how that reference interacts with the reference to probability in the recognition criteria.

The IASB also discussed whether to remove the term 'probable' from the recognition criteria:

- a. The IASB tentatively agreed that the Discussion Paper should explain the difference between uncertainty about whether an asset or liability exists (sometimes called 'existence uncertainty' or 'element uncertainty') and uncertainty of outcome.
- b. Uncertainty over the existence of the asset or liability: in most cases, it is clear whether an asset or liability exists, but in some cases this may be uncertain. The IASB tentatively decided that the Discussion Paper will discuss the different approaches for such cases. The issues to be considered include whether to apply an explicit probability threshold in such cases, what the threshold should be (eg virtually certain, probable) and whether the threshold for an asset should be the same as for a liability.

- c. Uncertainty of outcome: the IASB tentatively decided that although an asset or a liability must be capable of generating inflows or outflows of economic benefits, there is no minimum probability threshold that those inflows or outflows must reach before a resource or an obligation qualifies for recognition as an asset or a liability.

ASAF members discussed the approach to uncertainty in the definition and recognition of assets and liabilities and made the following comments:

- a. Many ASAF members thought that the term 'expected' in the definitions of an asset or liability was confusing and preferred the suggested replacement, 'capable'. However, others were concerned about removing reference to probability from the definitions of an asset and liabilities because they believed it could result in an entity searching for assets or liabilities that have very little chance of producing an inflow or outflow of economic benefit for the entity.
- b. ASAF members agreed that it was important to make a distinction between uncertainty of existence and uncertainty of outcome.
- c. Some recommended that the discussion paper should include some examples that illustrate the effect of removing the term 'expected' from the definitions of an asset or liability and of removing references to probability from the recognition criteria. They felt that such examples would make it easier for respondents to assess the possible effects on projects to develop or amend standards. However other members cautioned against using too many examples in the Conceptual Framework because it would be difficult to deal at a conceptual level with the details of particular transactions and could imply a proposed change to existing IFRSs.
- d. Some ASAF members suggested that some sort of probability threshold should be retained and that a different threshold should be applied to assets and liabilities (to reflect caution or prudence).
- e. Some expressed the view that both uncertainty of outcome and uncertainty of existence should be dealt with through measurement, and should not affect decisions about recognition.

Commenting on other proposed changes to the definitions of assets and liabilities:

- a. Some ASAF members stated that the recognition criteria should include reference to reliability.
- b. There were mixed views on whether the best place to include the notion of control was in the definition of an asset or in the recognition criteria. ASAF members noted that the staff are now proposing to include 'control' in the definition of an asset, rather than in the recognition criteria, to avoid unintended consequences.
- c. Some suggested that the discussion paper should explain in more detail whether goodwill meets the definition of an asset.
- d. Some suggested that the discussion paper should explain in more detail what the unit of account would be for forward contracts and executory contracts.

Other issues

ASAF members also had a short discussion on other areas of the Conceptual Framework issues. During the discussion they:

- a. provided suggestions for improving the arguments in the discussion paper; and
- b. suggested additional issues that should be covered.

Some members called for the concept of prudence (viewed as the exercise of caution under conditions of uncertainty) to be reinstated in the Conceptual Framework and for the IASB to explain the use of prudence in standard-setting (possibly as a change to the basis for conclusions on Chapter 3 of the existing Conceptual Framework). In addition, some members stated that, given the importance of the Conceptual Framework, the comment period for the discussion paper should be 6 months.

Impairment

IASB and ASAF Members

The IASB members responsible for supporting this project participated in this session: Hans Hoogervorst, Ian Mackintosh, Stephen Cooper and Martin Edelmann (Darrel Scott is also a Board Advisor on this project but he was not available for this meeting).

Mike Ashley joined the meeting as an EFRAG representative for this part of the meeting.

Overview

The ASAF held an education session on the IASB and US Financial Accounting Standards Board (FASB) proposals for expected credit losses.

The IASB staff presented a high-level summary of the proposals in the IASB exposure draft *Expected Credit Losses* that was published in March 2013. Leslie Seidman presented a high-level summary of the FASB proposals in its exposure draft *Financial Instruments—Credit Losses* that was published in December 2012. Hans Hoogervorst confirmed that re-deliberations would begin jointly in July and that both Boards would seek to achieve convergence if possible.

ASAF comments

ASAF members requested further clarification on the following matters:

- a. Some ASAF members requested further information about how the pattern of expected credit losses would affect the timing and amount of losses recognised under the IASB model; in particular, when the 'significant deterioration' criterion would be met if cash flows were back-end loaded;
- b. Some noted concerns regarding the amount of losses that would be recognised under the FASB model, noting that such amounts would be uneconomic to recognise from day 1;
- c. One member requested clarification regarding the interaction of a non-accrual interest recognition approach with the measurement of amounts at a present value under the FASB model;
- d. One member was concerned that limiting the assessment of significant deterioration to a probability of default may result in unintended consequences if expected losses increased as a result of a change in the loss given default and not the probability of default; and
- e. Some ASAF members expressed concerns regarding the level of subjectivity of both proposals.

ASAF members noted that their organisations had still to consider the proposals in depth and requested that they hold a conference call closer to the comment letter deadline to explore the issues further and any potential for convergence between the two approaches.

Next meeting

The next meeting will be held in London on 25 and 26 September 2013.

¹ The MoU is at: <http://www.ifrs.org/The-organisation/Advisory-bodies/Documents/20130408-MoU-Signed.pdf>