



Memorandum

To:	AASB members	Date:	1 July 2014
From:	Sue Lightfoot	Agenda Item:	18.1 (M139)
Subject:	IFRS Quality Control	File:	

Action

Consider EFRAG's invitation to comment on proposals to enhance IFRS quality control and decide whether to respond to EFRAG or the IASB at this stage.

Attachments

Agenda Paper 18.2 – EFRAG draft letter and Invitation to Comment

Background

On 6 June 2014, the European Financial Reporting Advisory Group (EFRAG) published a draft letter and Invitation to Comment seeking views on its proposal to enhance IASB quality control procedures at the stage of finalising a standard. EFRAG has requested comment by 15 August 2014.

In the draft letter, EFRAG proposes changes to the standard setting process at the stage of finalising an International Financial Reporting Standard (IFRS) in order to address difficulties¹ of interpretation and implementation that may arise once a standard has been released.

EFRAG proposes that amendments and clarifications during an implementation period of a standard should benefit from a 'lighter due process' in order to allow for greater responsiveness by the IASB in removing uncertainties and operational difficulties.

Public 'Fatal Flaw' Drafts

In the draft letter EFRAG supports the use of public 'fatal flaw' drafts and recommends that the results of public fatal flaw drafts should be assessed in a public meeting before final decisions are made. EFRAG also proposes that final balloting only takes place after public fatal flaw review and appropriate field testing.

The publication of the IASB's review draft of the general hedge accounting requirements of IFRS 9 *Financial Instruments* in September 2012 is cited as a successful use of the review draft process.

¹ The draft letter cites, by way of example, implementation problems of IFRS 11 *Joint Arrangements* and the lengthy consultation period on the second exposure draft on *Revenue from Contracts with Customers*.

Transition Resource Groups

The draft EFRAG letter notes the establishment by the IASB and FASB of a Joint Transition Group for Revenue Recognition (TRG)² to support implementation of IFRS 15 *Revenue from Contracts with Customers* which was issued in May 2014. The first meeting of the TRG is scheduled for 18 July 2014.

Although the TRG will hold public meetings, chaired by IASB and FASB members, it will not issue guidance. EFRAG notes that changes to the standard will follow the normal due process.

AASB staff also note that on 23 June 2014 the IASB announced its intention to establish a Transition Resource Group for Impairment of Financial Instruments (ITG)³. The ITG is intended to be a support implementation of the forthcoming impairment requirements to be added to IFRS 9 *Financial Instruments*. Similar to the TRG, the ITG will also not issue guidance.

EFRAG's Proposal for an Implementation Phase Group

The draft EFRAG letter proposes that if the IASB does not include public fatal flaw review in its due process, it could instead insert an implementation stage for a specified period post publication of standards. EFRAG proposes that the IASB set up a group with authority similar to the IFRS Interpretations Committee (IFRS IC). The group would:

- issue statements similar to IFRS IC rejection notices, if it deems the standard is appropriate, or
- publish tentative changes in the drafting of the standard with explanations of clarifications given.

Constituents would have opportunity to comment. Before the end of the implementation stage an amended standard would be approved by the IASB without further due process. If material changes were deemed necessary, normal due process would be followed.

Invitation to Comment

The following questions are asked in EFRAG's invitation to comment:

- 1 Do you agree with EFRAG that some [further] specific standard setting process step involving the public at large is necessary to further enhance quality control of IFRS? Please explain your views.
- 2 Do you support the proposal made by EFRAG? Please explain your views.
- 3 Would you favour alternative proposals? If so, what are they?

Staff comments and recommendations

Staff acknowledge the challenges of implementing new accounting requirements and fully support consideration of improvements to the existing processes. We also note that the IFRS Foundation has

2 <http://www.ifrs.org/Current-Projects/IASB-Projects/Revenue-Recognition/Project-news-history/Pages/Project-update-June-2014.aspx>

3 <http://www.ifrs.org/Alerts/ProjectUpdate/Pages/IASB-to-establish-transition-resource-group-for-impairment-of-financial-instruments-June-2014.aspx>

a Due Process Oversight Committee (DPOC), which last updated the *IASB and IFRS Interpretations Committee Due Process Handbook* as recently as February 2013.

At this stage, staff recommend that the AASB does not respond to EFRAG's invitation to comment on its proposals, however staff recommend the following:

- 1 Staff support the use of public 'fatal flaw' review drafts by the IASB on a case-by-case basis, and support the IASB publicly assessing the findings. Staff are of the view that the IASB should retain discretion on whether a fatal flaw review is required, rather than mandating this as part of their due process. Staff recommend communicating this message to the IASB when the opportunity arises. We would expect that, before the DPOC would consider changing the due process in a material manner, it would conduct its own stakeholder engagement.
- 2 Staff have some concern about the establishment of transition groups for specific topics, and are also cognisant that further groups may be established, for example, on lease accounting and insurance contracts, as revised standards are issued on those topics. Staff note that the first meeting of the Revenue TRG is scheduled for 18 July 2014. At this stage, staff recommend monitoring the activities and output of the TRG before considering whether to provide comment to the IASB or the DPOC.
- 3 Staff do not support the establishment of implementation phase groups as proposed by EFRAG, in addition to the IFRS IC. Staff note that the criteria used by IFRS IC to place issues on its agenda and whether it receives useful feedback from stakeholders was discussed at the IFASS⁴ meeting in March 2014 (held in Delhi). Staff note that as a result, some improvements in process have already been made, for example in improved communication with the target audience when the IFRS IC conducts outreach. Staff recommend that the effectiveness of the IFRS IC remains a focus and if further specific comments are identified about the operations of the IFRS IC, these should be raised with the IFRS IC or the DPOC at that time.

Question to Board members:

Does the Board agree with the staff recommendations?

4 http://www.aasb.gov.au/admin/file/content102/c3/Report_of_IFASS_Meeting_March_2014.pdf