IFRIC Update

From the IFRS Interpretations Committee

IFRS

May 2015

Welcome to the IFRIC *Update*

IFRIC Update *is the newsletter of the IFRS Interpretations Committee (the 'Interpretations Committee'). All conclusions reported are tentative and may be changed or modified at future Interpretations Committee meetings.*

Decisions become final only after the Interpretations Committee has taken a formal vote on an Interpretation or a Draft Interpretation, which is confirmed by the IASB.

The Interpretations Committee met in London on **12 May 2015**, when it discussed:

- **Items on the current agenda**
  - IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*—Issues relating to the requirements for scope and presentation in IFRS 5 (Agenda Papers 3, 3A, 3B, 3C, 3D and 3E)
  - IFRS 11 *Joint Arrangements*—Becoming a joint operator through the acquisition of an additional interest in an existing joint operation (Agenda Paper 8)
  - IAS 16 *Property, Plant and Equipment*—Accounting for net proceeds and costs of testing for property, plant and equipment (Agenda Paper 2)
  - IAS 21 *The Effects of Changes in Foreign Exchange Rates*—Draft Interpretation *Foreign Currency Transactions and Advance Consideration:* sweep issue (Agenda Paper 11)
- **Item recommended to the IASB for Annual Improvements**
  - IAS 23 *Borrowing Costs*—Borrowing costs on completed qualifying assets (Agenda Paper 9)
- **Other matters**
  - IFRS 13 *Fair Value Measurement*—The fair value hierarchy when third-party consensus prices are used (Agenda Paper 5)
  - Interpretations Committee work in progress update (Agenda Paper 10)
- **Interpretations Committee agenda decisions**
  - IFRS 10 *Consolidated Financial Statements*—Single-asset, single-lessee lease vehicles
  - IAS 24 *Related Party Disclosures*—Definition of close members of the family of a person

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Future IFRS Interpretations Committee meetings

The next meetings are:

14 and 15 July 2015

8 and 9 September 2015

10 and 11 November 2015

Meeting dates, tentative agendas and additional details about the next meeting will be posted to the IASB **website** before the meeting. Further information about the activities of the IFRS Interpretations Committee can be found **here**. Instructions for submitting requests for Interpretations are given on the IASB website **here**.

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Items on the current agenda

At this meeting, the Interpretations Committee discussed the following items on its current agenda:

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*—Issues relating to the requirements for scope and presentation in IFRS 5 (Agenda Papers 3, 3A, 3B, 3C, 3D and 3E)

At its November 2014 and March 2015 meetings, the Interpretations Committee considered questions relating to the scope of IFRS 5. As a result of those discussions, the Interpretations Committee asked the staff to undertake a broader analysis of the scope of IFRS 5 to help the Interpretations Committee decide whether these scope issues should be addressed through an Interpretation, or whether a broader amendment to

IFRS 5 would be necessary. The Interpretations Committee also discussed new issues that it had received relating to various aspects of the requirements in IFRS 5. At this meeting, the Interpretations Committee discussed the following issues:

(a) Issue 1: the scope of the held-for-sale classification;

(b) Issue 2: how to present intragroup transactions between continuing and discontinued operations;

(c) Issue 3: applicability of the disclosure requirements in IFRS 12 *Disclosure of Interests in Other Entities* to a subsidiary classified as held for sale;

(d) Issue 4: to what extent an impairment loss can be allocated to non-current assets within a disposal group; and

(e) Issue 5: how to apply the presentation requirements, in the case of a change to a sale plan, to a disposal group that consists of both a subsidiary and other non-current assets.

General decision reached at this meeting

As a result of its discussions, the Interpretations Committee decided that a summary of the IFRS 5 related issues that it had discussed should be included in a paper that would be referred to the IASB. The purpose of the paper would be to summarise, and categorise, the IFRS 5 issues to see if the IASB thought any matters should be addressed through the normal processes of the Interpretations Committee or whether the IASB thought it would be better to consider undertaking a broader project on IFRS 5.

The following sections within this topic represent what the Interpretations Committee observed and noted with respect to the individual issues that it discussed at this meeting.

Issue 1: the scope of the held-for-sale classification

The Interpretations Committee noted that the original scope of the held-for-sale classification in IFRS 5 was narrow and that it included only sale transactions. The Interpretations Committee also observed that several amendments to the scope of IFRS 5 had emphasised that:

(a) the loss of control is a significant economic event and thus establishing the intention to lose control, which meets the IFRS 5 evidential requirements, triggers the held-for-sale classification provided other relevant criteria are met; and

(b) the focus on the method of recovery of the carrying amount of non-current assets (or disposal groups) had changed from sale transactions to a method other than continuing use.

Consequently, the Interpretations Committee observed that the current objective for the scope of the held-for-sale classification in IFRS 5 is to capture non-current assets (or disposal groups) over which an entity is committed to lose control, irrespective of the form of the transaction (other than abandonment). The Interpretations Committee also reaffirmed that such classification must be supported by the fact that non-current assets (or disposal groups) to be disposed of must be available for immediate disposal, and it is highly probable that the entity will lose control.

Issue 2: how to present intragroup transactions between continuing and discontinued operation

The Interpretations Committee noted that there are no requirements or guidance in IFRS 5 or IAS 1 *Presentation of Financial Statements* in relation to the presentation of discontinued operations, which override the consolidation requirements in IFRS 10 *Consolidated Financial Statements*. Consequently, the Interpretations Committee tentatively concluded that an entity is required to eliminate intragroup transactions in full prior to determining the presentation of continuing and discontinued operations. Referring to paragraph 30 of IFRS 5, the Interpretations Committee also noted that entities may have to provide disclosures as necessary in order to enable users of financial statements to evaluate the financial effects of discontinued operations.

Issue 3: applicability of the disclosure requirements in IFRS 12 Disclosure of Interests in Other Entities *to a subsidiary classified as held for sale*

The Interpretations Committee discussed whether the disclosure requirements in IFRS 12 apply to non-current assets (or disposal groups) that are classified as held for sale or discontinued operation in accordance with IFRS 5. The question arises because paragraph 5B of IFRS 5 states that the disclosure requirements of another Standard do not apply unless that Standard specifically requires disclosures in respect of such assets.

Paragraph B17 of IFRS 12 specifically exempts an entity from the disclosure requirements in paragraphs B10–B16 of IFRS 12 if those investments are within the scope of IFRS 5. The Interpretations Committee observed that IFRS 12, when read in isolation, might imply that the disclosure requirements in IFRS 12 other than those in paragraphs B10–B16 of IFRS 12 would apply to investments within the scope of IFRS 12 that are classified as held for sale. However, the Interpretations Committee noted that even if this was what the IASB intended when it issued IFRS 12, paragraph 5B of IFRS 5 is clear and IFRS 12 does not include a reference to IFRS 5 in relation to the any other specific IFRS 12 disclosure requirements. This issue will be raised with the IASB.

Issue 4: to what extent an impairment loss can be allocated to non-current assets within a disposal group

Paragraph 23 of IFRS 5 addresses the recognition of impairment losses for a disposal group. In determining the order of allocation to non-current assets, paragraph 23 refers to paragraphs 104 and 122 of IAS 36 *Impairment of Assets* but not to paragraph 105 of IAS 36, which relates to the extent of an impairment loss that an entity can allocate to an asset. Consequently, the Interpretations Committee tentatively concluded that paragraph 105 of IAS 36 does not affect the allocation of an impairment loss for a disposal group to the assets.

The Interpretations Committee also noted that this issue is different from the other IFRS 5 measurement-related issues that the Interpretations Committee had previously looked at, because this issue relates only to the measurement of non-current assets that are within the measurement scope of IFRS 5, whereas the other issues touch on the measurement of assets and liabilities, including those that are not within the measurement scope of IFRS 5.

Issue 5: how to apply the presentation requirements, in the case of a change to a sale plan, to a disposal group that consists of both a subsidiary and other non-current assets

The Interpretations Committee discussed two issues in relation to the requirements in paragraph 28 of IFRS 5:

(a) when a disposal group consists both of a subsidiary, joint operation, joint venture, associate, or a portion of an interest in a joint venture or an associate, and other non-current assets, the guidance in paragraph 28 of IFRS 5 suggests that the effect of re-measurement upon a change in a sale plan on different parts of the disposal group is reflected in different periods.

(b) it is not clear on whether a retrospective amendment as required by paragraph 28 of IFRS 5 applies only to measurement or also applies to presentation, with respect to a change of a sale plan involving a subsidiary, joint operation, joint venture, associate, or a portion of an interest in a joint venture or an associate.

With respect to Issue 5(a), the Interpretations Committee noted that the requirements in paragraph 28 are inconsistent, because when there has been a change to a sale plan, paragraph 28 of IFRS 5 requires the effects of a re-measurement of a disposal group that is a subsidiary, joint operation, joint venture, associate, or a portion of an interest in a joint venture or an associate, to be recognised retrospectively, whereas it requires the effects of a re-measurement of non-current assets to be recognised in the current period.

With respect to Issue 5(b), the Interpretations Committee observed that the requirements in IFRS 5 are not clear on whether the term ‘amended accordingly’ in paragraph 28 of IFRS 5 refers only to measurement or whether it also refers to presentation when there has been a change to a sale plan.

The Interpretations Committee tentatively decided that the possibility of amending the Standard to address the concerns noted in Issues 5(a) and (b) should be discussed with the IASB.

IFRS 11 *Joint Arrangements*—Becoming a joint operator through the acquisition of an additional interest in an existing joint operation (Agenda Paper 8)

The Interpretations Committee received a request to clarify whether a previously held interest in the assets and liabilities of a joint operation is remeasured to fair value when the investor’s acquisition of an additional interest results in the investor becoming a joint operator (ie assuming joint control) in the joint operation. In this specific fact pattern, the activities of the joint operation constituted a business as defined by IFRS 3 *Business Combinations*. Prior to the acquisition of additional interests, the investor participated in, but did not have joint control of, the joint operation and the investor had rights to the assets and obligations for the liabilities. Accordingly, the investor recognised its share of the assets, liabilities, revenues and expenses from the joint operation in accordance with other Standards, as required by paragraph 23 of IFRS 11.

The Interpretations Committee understood that there are different views on whether or not the previously held interests in the assets and liabilities of the joint operation should be remeasured. The Interpretations Committee noted that some respondents to the outreach also highlighted other transactions involving previously held interests in which there were different views on the remeasurement of such interests. The Interpretations Committee observed that it would be useful to analyse these other transactions simultaneously with the fact pattern that had been submitted.

Next steps

To assist the Interpretations Committee with determining the appropriate scope of the project, the staff will present a paper at a future meeting identifying other transactions in which there is a perceived lack of guidance or where diversity in practice may exist in determining the appropriate accounting for previously held interests.

IAS 16 *Property, Plant and Equipment*—Accounting for net proceeds and costs of testing for property, plant and equipment (Agenda Paper 2)

The Interpretations Committee received a request to clarify the accounting for the net proceeds from selling items produced while testing an item of property, plant and equipment (PPE) under construction, ie as part of the activities necessary to bring the item of PPE to the location and condition necessary for it to be capable of operating in the manner intended by management. The submitter has asked whether the amount by which the net proceeds received exceed the costs of testing should be recognised in profit or loss or as a deduction from the cost of the PPE.

In January 2015 the Interpretations Committee observed that the analysis should focus on the meaning of 'testing' the PPE, because the deduction of proceeds is stated only in relation to testing in paragraph 17(e) of IAS 16. On this basis, whether the proceeds should be deducted from the cost of the PPE would be determined depending on whether the activity that led to those proceeds was testing. The Interpretations Committee also observed that the disclosure about this issue is important and should be considered.

At this meeting, the Interpretations Committee discussed the analysis on the meaning of testing and whether disclosure requirements should be added.

Meaning of testing

The Interpretations Committee discussed whether the clarification of the meaning of testing should be made as an amendment to IAS 16 or by developing an Interpretation. The Interpretations Committee tentatively decided to develop an Interpretation on the meaning of testing, focussing on the meaning of 'functioning properly' in paragraph 17(e) of IAS 16. The Interpretations Committee considered that functioning properly reflects the technical/physical performance of the PPE, and is not the financial performance such as the level of operating margin or quantity of the output as intended by management.

Disclosure

The Interpretations Committee also discussed whether any additional disclosure requirements should be developed. The Interpretations Committee considered that, if material, the quantitative disclosure on the amount of proceeds that has been deducted from the PPE is important for users to understand the effect on the financial statements. The Interpretations Committee tentatively decided that this disclosure requirement would be included in the proposed Interpretation by referencing the existing disclosure requirement in paragraph 73(e)(ix) of IAS 16, which requires the disclosure of other changes in PPE. Some of the Interpretations Committee members expressed the view that other disclosures such as amounts recognised in profit or loss also need to be disclosed.

The staff will prepare the draft Interpretation and present it at a future meeting.

IAS 21 *The Effects of Changes in Foreign Exchange Rates*—Draft Interpretation *Foreign Currency Transactions and Advance Consideration:* sweep issue (Agenda Paper 11)

The Interpretations Committee continued its discussions on the development of an Interpretation of paragraphs 21–22 of IAS 21. The proposed guidance addresses how to determine the date of the transaction for the purposes of IAS 21. The date of the transaction determines the spot exchange rate used to translate a foreign currency transaction on initial recognition of the asset, expense or income (or part of it) that follows the recognition of a non-monetary prepayment asset or a non-monetary deferred income liability.

At this meeting, the Interpretations Committee considered the interaction of the proposed draft Interpretation and the presentation in profit or loss of exchange differences arising on monetary trade receivable or trade payable balances.

Subsequent to the initial recognition of a foreign currency balance sheet item, paragraphs 28–29 of IAS 21 require that exchange differences arising on the settlement of monetary items or on translating monetary items at the end of the reporting period should be recognised in profit or loss in the period in which they arise (subject to a few specified exceptions). The Interpretations Committee noted that IFRS does not specify in which line item within profit or loss such exchange differences should be presented.

However, the concern raised to the Interpretations Committee was that the proposed draft Interpretation implies that such exchange differences should not be recognised in the same line item as the foreign currency transaction. This is because it specifies the exchange rate to use to recognise a foreign currency transaction that is recognised in profit or loss.

In developing the proposed draft Interpretation, the Interpretations Committee did not intend to address exchange differences arising on the subsequent retranslation of monetary items, nor did it intend to address in which line item such exchange differences should be recognised.

Thirteen of the fourteen members of the Interpretations Committee tentatively decided not to include a discussion about the presentation of exchange differences arising on the settlement or retranslation of monetary items in the Basis for Conclusions of the draft Interpretation. Their reasoning was that it is not relevant to the issue being addressed by the proposed Interpretation, which is the meaning of the 'date of the transaction' for the purposes of the initial recognition of a foreign currency transaction in the functional currency in accordance with paragraph 21 of IAS 21. The presentation of foreign exchange gains and losses arising subsequent to the date of the transaction is not relevant to the date of the measurement of the foreign currency transaction in the functional currency on initial recognition.

The Interpretations Committee reconfirmed their general agreement that the staff should prepare the draft Interpretation for a written ballot, subject to no significant matters arising from discussions at the IASB (thirteen members of the Interpretations Committee agreed). One member voted against the proposal. The staff noted that in accordance with the IFRS Foundation's *Due Process Handbook*, the Basis for Conclusions to the draft Interpretation will identify any areas in which some members of the Interpretations Committee hold strong views in opposition to the draft Interpretation.

Next steps

The staff will present a paper to the IASB at one of its future meetings, which will summarise the technical analysis and due process that the Interpretations Committee has undertaken to develop the proposed draft Interpretation.

If no significant matters arise from discussions at the IASB meeting, the staff will prepare the draft Interpretation for a written ballot.

Item recommended to the IASB for Annual Improvements

The Interpretations Committee assists the IASB in Annual Improvements by reviewing proposed improvements to Standards and making recommendations to the IASB. Specifically, the Interpretations Committee's involvement includes reviewing and deliberating issues for their inclusion in future Exposure Drafts of proposed Annual Improvements to IFRS *and deliberating the comments received on the Exposure Drafts. When the Interpretations Committee has reached consensus on an issue included in* Annual Improvements to IFRS*, the recommendation (including finalisation of the proposed amendment or removal from Annual Improvements) will be presented to the IASB for discussion, in a public meeting, before being finalised. Approved* Annual Improvements to IFRS *(including Exposure Drafts and final Standards) are issued by the IASB.*

IAS 23 *Borrowing Costs*—Borrowing costs on completed qualifying assets (Agenda Paper 9)

The Interpretations Committee received a request to clarify whether funds borrowed specifically to finance the construction of a qualifying asset, the construction of which has now been completed, must be included as part of the general borrowings for the purposes of determining the capitalisation rate for qualifying assets that have been funded from the entity's general borrowings. The submitter described a scenario in which an entity borrows funds specifically to finance the construction of a qualifying asset. Subsequently, the activities necessary to prepare the asset for its intended use or for sale were completed, but the funds have not been repaid. The submitter notes that this is a common scenario and could arise in group situations. It could also arise in instances in which an entity wishes to maintain a specified level of borrowings for an optimal capital structure amongst others.

The submitter asked whether the funds borrowed specifically to finance the construction of a qualifying asset should be included within the general borrowings after the construction of the specific asset is completed. The consequence of including these funds within the general borrowings is that the interest rate on the borrowings would be included in the calculation of the capitalisation rate to be applied to other qualifying assets that have been funded from general borrowing sources as described in paragraph 14 of IAS 23.

When determining the capitalisation rate to be applied to qualifying assets that have been funded from general borrowings, paragraph 14 of IAS 23 requires an entity to use the weighted average of the borrowing costs applicable to 'the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purposes of obtaining a qualifying asset'. On the basis of the wording in paragraph 14 of IAS 23, a majority of the Interpretations Committee tentatively agreed with the staff conclusion that the specific borrowings should be included within the general borrowings in the fact pattern described by the submitter.

However, the Interpretations Committee noted that there is diversity in practice, which arises from a perceived lack of clarity in the wording in paragraph 14 of IAS 23. The Interpretations Committee tentatively decided that the wording in IAS 23 should be clarified through an annual improvement. The staff will present the proposed improvement at a future meeting.

Other matters

IFRS 13 *Fair Value Measurement*—The fair value hierarchy when third-party consensus prices are used (Agenda Paper 5)

The Interpretations Committee was presented with the results of the outreach undertaken in relation to the final agenda decision in January 2015 pertaining to IFRS 13 *Fair Value Measurement*—The fair value hierarchy when third-party consensus prices are used. The feedback was provided for information purposes only and addressed the additional questions that were raised during the finalisation of the agenda decision. The Interpretations Committee noted the results of the outreach and determined that no further work was necessary.

Interpretations Committee work in progress update (Agenda Paper 10)

The Interpretations Committee received a report about ongoing issues that were not discussed at this meeting.

Interpretations Committee agenda decisions

The following explanations are published for information only and do not change existing IFRS requirements. Interpretations Committee agenda decisions are not IFRIC Interpretations. IFRIC Interpretations are determined only after extensive deliberations and due process, including a formal vote, and become final only when approved by the IASB.

IFRS 10 *Consolidated Financial Statements*—Single-asset, single-lessee lease vehicles

The Interpretations Committee received two requests for clarification about the interaction of IFRS 10 and IAS 17 *Leases*. In both examples, a structured entity (SE) is created to lease a single asset to a single lessee.

In one submission the lease is an operating lease; in the other it is a finance lease. In the case of the operating lease, the question was whether the lessee should consolidate the SE. In the case of the finance lease, the question was whether the lender should consolidate the SE. In both examples, the consolidation decision would be based on an assessment of whether the entity controls the SE. In particular, the submitters asked whether the lessee's use of the leased asset is a relevant activity of the SE when assessing power over the SE.

The Interpretations Committee noted that an entity has power over an investee when it has rights that give it the current ability to direct the relevant activities of the entity, ie the activities that significantly affect the investee's returns. On entering into a lease, regardless of whether it is a finance lease or an operating lease, the SE (the lessor) would have two rights—a right to receive lease payments and a right to the residual value of the leased asset at the end of the lease. Consequently, the activities that would affect the SE's returns would relate to managing the returns derived from these rights; for example, managing the credit risk associated with the lease payments and any other guaranteed payments or managing the leased asset at the end of the lease term (for example, managing its sale or re-leasing). How the decision-making relating to these activities would significantly affect the SE's returns would depend on the particular facts and circumstances.

The Interpretations Committee was of the view that the lessee's right to use the leased asset for a period of time would not, in isolation, typically give the lessee decision-making rights over these relevant activities of the SE and hence would not typically be a relevant activity of the SE.

However, it noted that this conclusion does not mean that a lessee can never control the lessor. For example, a parent that controls another entity for other reasons can lease an asset from that entity.

It also noted that, in assessing control, an entity would consider all of the rights that it has in relation to the investee to determine whether it has power over the investee. This would include rights in contractual arrangements other than the lease contract, such as contractual arrangements for loans made to the lessor, as well as rights included within the lease contract, including those that go beyond simply providing the lessee with the right to use the asset.

As a result of its discussions, the Interpretations Committee concluded that the principles and guidance within IFRS 10 would enable a determination of control to be made in a specific scenario based on the relevant facts and circumstances of that scenario. The Interpretations Committee also noted that it is not its practice to give case-by-case advice on individual fact patterns.

Consequently, the Interpretations Committee thought that neither an Interpretation of nor an amendment to a Standard is required and decided not to add these issues to its agenda.

IAS 24 *Related Party Disclosures*—Definition of close members of the family of a person

The Interpretations Committee received a submission regarding the definition of close members of the family of a person in paragraph 9 of IAS 24.

The submitter points out that the definition of close members of the family of a person in paragraph 9 does not specify that the parents of a person could be included in this definition. The submitter thinks that this definition should include a person's parents, because in its view they are among the closest members of the family of a person who may be expected to influence, or be influenced by, that person in their dealings with the entity. The submitter further observes that local regulations in some jurisdictions include the parents of a person within the definition of 'close members of the family of a person'.

The submitter suggests that the Interpretations Committee could:

(a) specify that this definition includes 'persons who are considered to be close members of the family according to the law or the prevailing customary norms in the jurisdiction where the entity operates'; and

(b) remove the examples of 'close members of the family of a person' from the definition.

The Interpretations Committee observed that the definition of close members of the family of a person in paragraph 9 of IAS 24:

(a) is expressed in a principle-based manner and involves the use of judgement to determine whether members of the family of a person (including that person's parents) are related parties or not; and

(b) includes a list of family members that are always considered close members of the family of a person.

The Interpretations Committee further noted that the list of family members in paragraph 9(a)–(c) is non-exhaustive and does not preclude other family members from being considered as close members of the family of a person. Consequently, the Interpretations Committee thought that other family members, including parents or grandparents, could qualify as close members of the family depending on the assessment of specific facts and circumstances.

In the light of the existing IFRS requirements, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary and therefore decided not to add this issue to its agenda.

Welcome

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