



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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DATE: 15 OCTOBER 2003
MEMO TO: MEMBERS OF THE IFAC PUBLIC SECTOR COMMITTEE
FROM: MATTHEW BOHUN & HONGXIA LI
SUBJECT: STATUS OF IASB PROJECTS AS AT SEPTEMBER 2003

ACTION REQUIRED

The Committee is asked to note the update on the IASB work program.

AGENDA MATERIAL:

	Pages
Appendix 1 IASB Projects Timetable	6.32
Appendix 2 IASB Illustrative Example of Proposed format for Performance Reporting	6.33

BACKGROUND

On 9 October 2003, the IASB published an updated the timetable for its projects on its active agenda. The timetable (Appendix 1) shows the IASB's current expectations about the timing of these projects.

This memorandum provides an update of developments in the IASB's work program since the PSC meeting in Vancouver in July 2003. Any projects of the IASB that are not mentioned in this memo are unlikely to be of great relevance to the public sector, e.g. earnings per share.

PROJECTS

(i) Improvement Projects

The IASB aims to conclude by the end of 2003 its work on:

- revising the 12 IASs included in the *Exposure Draft of Proposed Improvements to Existing International Accounting Standards*; and
- revising the 2 IASs on financial instruments (except for the limited amendment to IAS 39, on *Fair Value Hedge Accounting For A Portfolio Hedge of Interest Rate Risk* and expected to be issued in the first quarter of 2004).

The IASB intends that these revised versions should be applied for annual periods beginning on or after 1 January 2005. The Improvements project is discussed in more detail in agenda Item 14 *IPSAS Review and Update – Harmonization with IFRS*.

(ii) Provisions, Contingent liabilities and Contingent Assets

At its September 2003 meeting, the IASB continued its consideration of proposed amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* arising from its Business Combinations phase II project. The IASB discussed examples of items that would meet the current definition of a contingent liability in IAS 37.

At the July meeting in Vancouver, staff reported that the IASB had tentatively agreed to amend the definition of “contingent liability”. At its September meeting, the IASB tentatively agreed that the definition should be further amended as follows:

A contingent liability is:

~~a possible conditional obligation that arises from past events and whose existence will be confirmed only the outcome of which will be resolved by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise entity.~~

~~(b) a present obligation that arises from past events but is not recognized because:~~

~~(i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or~~

~~(ii) the amount of the obligation cannot be measured with sufficient reliability.~~

If and when a final decision is made to amend the definition of contingent liabilities, it will have implications for IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, which uses the same definition. However, no final decisions have been made to date.

For this project summary, please link to <http://www.iasb.org.uk/docs/projects/converge-ps.pdf>.

(iii) Performance Reporting

At its June and July meetings, the IASB discussed the implications of the feedback received from field tests of its proposed comprehensive income statement format. Appendix 2 shows the proposed format. The following tentative decisions were made:

Financial and financing

- (a) A subtotal ‘business profit’ should not be required (i.e. there should not be a requirement for a sub-total of operating, other business profit and financial income, before financing expenses). The rationale was that it is preferable to permit preparers to present the comprehensive income statement in a manner that most closely reflects the way the entity is managed. Previously, the ‘business profit’ subtotal was required, irrespective of whether the entity operated its financing activities as a separate activity center.
- (b) Entities should be allowed a choice of subtotals between either the “other business profit” subtotal or a total of the “operating profit” and “other business profit”

categories (this could be termed “profit before financial income” or something similar).

Function vs. nature

Entities will not be required to report by function or by nature, nor be prohibited a mixed presentation – previously it was proposed that entities be required to report by function.

“Comprehensive income”, “statement of comprehensive income” and “before remeasurements” should be used as working terms for, respectively, the bottom line, the statement and the middle column.

Presentation on the face of the statement

Presentation of all three columns on the face of the statement should be mandatory for the reporting period, but not for comparatives. For comparatives, entities would be permitted to present the total column on the face, and the other columns in the notes.

For this project summary, please link to <http://www.iasb.org.uk/docs/projects/rci-ps.pdf>.

(iv) Revenue Recognition

At its June, July and September meeting, the IASB continued to consider the revenue recognition project and focused on two main topics:

- a proposed conceptual model for analyzing whether assets and liabilities arise from contractual rights and obligations and how to measure those assets and liabilities; and
- an ASB paper *Revenue Recognition: the EITF Approach, the Wholesale Approach and the Retail Approach*.

Basic features of the proposed Conceptual Model

The proposed Concept Model distinguishes between the following three types of contractual rights and obligations:

- (a) *conditional* —performance is subject to the occurrence of an event that is not certain to occur (such as performance by the counterpart to the contract);
- (b) *unconditional* —nothing other than the passage of time is required to make performance due; and
- (c) *mature* —performance is not subject to any event, not even the passage of time. It is due immediately.

The IASB generally supported the proposed conceptual model and tentatively agreed that:

- (i) conditional rights and obligations do not meet the definitions of an asset and a liability;
- (ii) unconditional rights and mature rights meet the definition of an asset if they are enforceable and give access to future economic benefits; and
- (iii) unconditional obligations and mature obligations meet the definition of a liability if they are enforceable and oblige the entity to make a future sacrifice of economic benefits.

The IASB has tentatively agreed to define revenues in terms of an increase in equity; therefore recognizing changes in net assets is necessary for recognizing and measuring revenue.

ASB paper *Revenue Recognition: the EITF Approach, the Wholesale Approach and the Retail Approach*

At its September meeting, the IASB discussed the UK Accounting Standards Board's (ASB) paper *Revenue Recognition: The EITF Approach, the Wholesale Approach and the Retail Approach*, which was prepared at the IASB's request.

The ASB paper discussed whether the fair value of a contractual obligation to a customer should be determined in the wholesale or retail market, and the implications of that choice for the timing of revenue recognition. The case studies in EITF Issue 00-21 *Revenue Arrangements with Multiple Deliverables* are used to illustrate these approaches to measuring fair value, and assumed that payment was received from the customer upon entry into the contract.

The IASB discussion was for information only and no Board decisions were made.

For this project summary, please link to <http://www.iasb.org.uk/docs/projects/revenue-ps.pdf>. Further information about the ASB paper is available in the IASB's observer's notes for the September 2003 meeting, linked here:

<http://www.iasb.org.uk/docs/bdpapers/2003/0309ob11.pdf>.

(v) Consolidation Including Special Purpose Entities

At its June 2003 meeting, the IASB considered a draft project plan for the consolidation project, which includes consolidation of special purpose entities (SPEs). It was noted that the project would result in an IFRS replacing IAS 27 *Consolidated Financial Statements*. (IAS 27 is included in the Improvements project and a [draft] IAS 27 *Consolidated and Separate Financial Statements* was included in the Improvements ED. It is scheduled to be issued by the end of 2003. If the improved IAS 27 were adopted, it would be further amended by this consolidation project.) Ultimately, the standard would address consolidation of both SPEs and non-SPEs. The IASB also agreed that the project should begin by considering the definition of control to be used as the basis for consolidation in the new standard.

At its September 2003 meeting, the IASB focused on the concept of "control" for non-SPEs and made the tentative decision that the concept of "control" should require satisfaction of three criteria:

- the ability to set strategic direction and to direct financing and operating policy and strategy (the '**Power Criterion**');
- the ability to access benefits (the '**Benefit Criterion**'); and
- the ability to use such power so as to increase, maintain or protect the amount of those benefits.

It was emphasized that determining whether control exists will depend on the circumstances of each case. The IASB also tentatively agreed that irrespective of the form of control, if the

control criteria are satisfied, consolidation should be required. A controlling entity need not have a minimum level of ownership.

The tentative decision made in this meeting will be used as a basis for considering when SPEs should be consolidated.

Final decisions on this project may have implications for IPSAS 6 if a new IFRS (replacing the current or proposed improved IAS 27) based on this project is issued.

For this project summary, please link to <http://www.iasb.org.uk/docs/projects/consolidation-ps.pdf>.

(vi) Disclosures of Risks Arising From and Other Disclosures Relating to Financial Instruments

At its July 2003 meeting, the IASB considered a proposed Standard and Implementation Guidance prepared by the Financial Activities Advisory Group. The proposed Standard builds on the principle that an entity should disclose information that enables users of its financial statements to evaluate the nature and extent of risks to the entity arising from financial instruments held during the reporting period and at the reporting date.

The scope of this project originally focused on revising IAS 30 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*. The IASB tentatively decided that the Standard should generally apply to all entities that hold financial instruments, not solely financial institutions, and confirmed its support for the Advisory Group's proposals.

The IASB tentatively agreed that a proposed Standard and related amendments are to be published for public comment in mid-2004 and issued early in 2005. The proposed Standard and other amendments would be effective for accounting periods beginning after 1 January 2007, with earlier adoption permitted or encouraged.

For this project summary, please link to <http://www.iasb.org.uk/docs/projects/deposit-ps.pdf>.

Appendix 1: IASB Projects Timetable

The IASB's expectations as at 9th October 2003 about the timing of projects on its active agenda

	2003	2004	
	Qtr 4	Qtr 1	Later
Improvements to existing International Financial Reporting Standards	IFRSs		
Amendments to IAS 32 <i>Financial Instruments: Disclosure and Presentation</i> and IAS 39 <i>Financial Instruments: Recognition and Measurement</i>	IFRSs		
<ul style="list-style-type: none"> IAS 39 - limited amendment: <i>Fair value hedge accounting for a portfolio hedge of interest rate risk</i> 		IFRS	
Financial risk and other amendments to financial instruments disclosures			EDs
Business combinations, <i>Phase I</i>		IFRSs	
Share-based payment		IFRS	
Reporting comprehensive income ¹			
Business combinations <i>Application of the purchase method</i>	ED		IFRS
Exploration and evaluation activities	ED		IFRS
Insurance contracts <i>Phase I</i>		IFRS	
Insurance contracts <i>Phase II</i>			ED
Concepts - revenue, liabilities and equity			ED
Consolidation and special purpose entities			ED
Short-term convergence of International Financial Reporting Standards and other national accounting standards			
-- Joint project with FASB (phases I and II)	EDs (I&II)	IFRS (I)	IFRSs (I&II)
-- Employee benefits ¹			
-- Replacement of IAS 20			ED

¹ timing under review

Legend: ED- Exposure Draft

IFRS - International Financial Reporting Standard

Appendix 2:

IASB Illustrative Example of Proposed Format for Performance Reporting¹

	Total	Before remeasurements	Remeasurements
Revenue	1000	1000	-
Write-down of accounts receivable	(10)	-	(10)
Cost of sales	(400)	(340)	(60)
Selling, general, admin	(250)	(200)	(50)
Operating Profit	340		
Disposal gain/loss	100	-	100
PPE revaluation	150	-	150
Investment property	-	-	-
Goodwill	(100)	-	(100)
FX gain/loss on net investment	(50)		(50)
Other Business Profit	100		
Income from associates	50	50	-
Equity investments	(60)	-	(60)
Debt investments	20	5	15
Pension assets	(150)	-	(150)
Financial Income	(140)		
Business Profit	300		
Interest on liabilities	(80)	(120)	40
Pension financing expenses	(120)	(200)	80
Financing expense	(200)		
Tax	(30)	-	-
Discontinued operations	(10)	(5)	(5)
Cash flow hedges	50	-	50
<u>Comprehensive Income</u>	(110)		

¹ Version 7.

Item 6.8 *The Status of IASB Projects as at September 2003*

PSC Berlin November 2003