



On the Horizon for IFRS

April 9, 2010

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IASB issues February 2 and 10, 2010 additional IASB and joint IASB/FASB meeting highlights

Key issues

At the February 2 and 10, 2010 additional IASB and IASB/FASB joint meetings the following issues were discussed:

- *Annual improvements*: the IASB reached a tentative decision to finalize six of the nine proposed improvements from the August 2009 Exposure Draft and expects to issue *Improvements to IFRSs* in April 2010

- *Financial instruments – classification and measurement*: the Boards discussed the classification and measurement of financial liabilities. The Boards agreed that liabilities that are not held to pay contractual cash flows should be measured at fair value through profit or loss. The IASB tentatively decided that financial liabilities that are held to pay contractual cash flows and that have “non-vanilla” contractual cash flow characteristics should be bifurcated into a host and embedded features.
- *Financial instruments – hedge accounting*: the Boards discussed but did not arrive at a decision on the objective for hedge accounting. The IASB tentatively decided to permit bifurcation-by-risk for financial items.
- *Insurance contracts*: the Boards reached tentative decisions on reinsurance and policyholder accounting
- *Leases*: the Boards tentatively decided that a lease would be defined as a contract that conveys the right to use a specified asset for a period of time in exchange for consideration
- *Presentation of other comprehensive income*: the Boards reached a tentative decision that the exposure draft, the FASB's proposed update on financial instruments, and the IASB's exposure draft on post-employment benefits would all be issued simultaneously in March 2010

The International Accounting Standards Board has issued an [IASB Update](#), which summarizes the additional IASB and joint IASB/FASB meetings that were held in London on February 2 and 10, 2010. The FASB participated via video conference for all sessions on February 2, 2010 and for the Insurance contracts and Financial instruments: classification and measurement sessions on February 10, 2010.

Highlights of the meetings are discussed below.

Annual improvements

Each year the IASB considers minor amendments to IFRS in an annual improvements project. The amendments represent non-urgent but necessary amendments to IFRS and are proposed each year in an omnibus Exposure Draft. The IASB approved the project plan and timetable for issuing *Improvements to IFRSs* in April 2010, which is based upon the Exposure Draft issued in August 2009.

Tentative approval of six proposed improvements

The IASB discussed nine of the proposed improvements to IFRS and reached a tentative decision to finalize six of the improvements.

IFRS 1, First-time Adoption of International Financial Reporting Standards – revaluation basis as deemed cost

The amendment extends the exemption in paragraph D8 to also apply to revaluations that occur during the period covered by the first IFRS financial statements but after the date of transition to IFRS, with the resulting adjustments at the measurement date recognized directly in retained earnings.

All decisions reached at IASB meetings are tentative and may be changed or modified at future meetings. Board decisions become final only after completion of a formal ballot to issue a Standard or Interpretation or to publish an Exposure Draft.

IFRS 3 (revised 2008), Business Combinations – measurement of non-controlling interests

The amendment clarifies that the choice for measuring the non-controlling interests (NCI) in the acquiree applies only to components of NCI that are present ownership instruments that entitle their holders to a proportionate share of the entity's net assets in the event of liquidation.

IFRS 3 (revised 2008), Business Combinations – transition requirements for contingent consideration from a business combination that occurred before the effective date of the revised IFRS

The amendment specifies that an entity should apply the requirements from IFRS 3 (issued 2004) as reproduced in the revised IFRS 3.

IFRS 7, Financial Instruments: Disclosures – clarification of disclosures

The amendment clarifies and amends the qualitative, quantitative, and credit risk disclosures.

IAS 28, Investments in Associates – partial use of fair value for measurement of associates

The amendment enables a parent entity to measure part of the investment in an associate at fair value in its consolidated financial statements when that part is designated as at fair value through profit or loss in accordance with the scope exclusion in paragraph 1 of IAS 28. The Board decided not to include in the forthcoming IFRS on joint arrangements equivalent guidance on the partial use of fair value for the measurement of investments in joint ventures.

IAS 34, Interim Financial Reporting – significant events and transactions

The amendment emphasizes disclosure principles and adds guidance on how to apply these principles.

Decision to remove three proposed amendments

The IASB decided to remove from the annual improvements project, without finalization, three proposed amendments that had been included in the *Improvements to IFRSs* exposure drafts in either August 2008 or August 2009. The Board decided that these issues should be reconsidered in conjunction with the broader project to replace IAS 39, *Financial Instruments: Recognition and Measurement* rather than on a piecemeal basis:

- IAS 27, *Consolidated and Separate Financial Statements* – impairment of investments in associates in the separate financial statements of the investor
- IAS 39 – Bifurcation of embedded foreign currency derivatives
- IAS 39 – Application of the fair value option

Issues to be discussed at March 2010 IFRIC and IASB meetings

At the March 2010 IFRIC and IASB meetings, the staff will present an analysis of the comment letters received for the following issues, which are included in the *Improvements to IFRSs* exposure draft issued in August 2009:

- IFRS 1 – Accounting policy changes in the year of adoption
- IFRS 3 – Unreplaced and voluntarily replaced share-based payment awards
- IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations* – application of IFRS 5 to a loss of significant influence over an associate or a jointly-controlled entity

- IAS 1, *Presentation of Financial Statements* – clarification of statement of changes in equity
- IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors* – change in terminology for the qualitative characteristics
- IAS 27 – transition requirements for amendments made as a result of IAS 27 (revised 2008) to IAS 21, IAS 28, and IAS 31
- IAS 40, *Investment Property* – change from fair value model to cost model
- IFRIC 13, *Customer Loyalty Programmes* – fair value of award credit

See the [IASB project summary](#) for more information on this project.

Financial instruments: classification and measurement

In IFRS 9, *Financial Instruments*, issued in November 2009, the IASB provided guidance on the classification and measurement of financial assets. Due to time constraints, the IASB elected to defer the discussion regarding financial liabilities. The FASB continued to move toward a comprehensive exposure draft on accounting for financial instruments.

At this joint meeting, the Boards began their discussion of how to measure financial liabilities. The staff grouped financial liabilities into three broad categories:

- Instruments that are not held to pay contractual cash flows (e.g. standalone derivatives and liabilities held for trading)
- Instruments that are held to pay contractual cash flows and have “non-vanilla” contractual cash flow characteristics (e.g. own debt that the entity holds to maturity whose payments are linked to an equity index)
- Instruments that are held to pay contractual cash flows and have “vanilla” contractual cash flow characteristics (e.g. instruments that do not contain embedded derivatives that require separate accounting)

The first two categories were discussed.

The Boards affirmed their previous tentative decisions that financial liabilities that are not held to pay contractual cash flows would be measured at fair value through profit or loss.

The IASB tentatively decided that financial liabilities that are held to pay contractual cash flows and have “non-vanilla” contractual cash flow characteristics would be bifurcated into a host and embedded features. Those components would be separately measured. This tentative decision responds to issues raised about recognizing gains or losses arising from changes in an entity's own credit risk. The tentative decision rejects the “frozen credit spread” method that some had advocated but was not supported by staff outreach efforts.

The FASB did not make any decisions about financial liabilities that are held to pay contractual cash flows that contain embedded derivatives. Under the FASB's current tentative model those liabilities would be measured at fair value with changes in fair value recognized in net income. The FASB will first consider whether and how to address changes in an entity's own credit risk for financial liabilities with “vanilla” contractual cash flow characteristics. Under the FASB's current tentative model, these changes would be required to be measured at fair value with changes in fair value recognized in other comprehensive income.

See the [IASB project summary](#) for more information on this project.

Financial instruments: hedge accounting

The Boards discussed possible objectives for hedge accounting and whether hedging by risk component (bifurcation-by-risk) should be permitted. The Boards have discussed principles-based objectives to hedge accounting but

were having difficulty agreeing with any of those proposed by the staff. No decision was made on the objective.

The IASB tentatively decided to permit bifurcation-by-risk for financial items and indicated a leaning toward permitting bifurcation-by-risk for non-financial items. Under a bifurcation-by-risk approach, the designation of a hedging relationship, and thus its effectiveness, is based on one or more but not all of the risks that can affect the hedged item's cash flows or its fair value.

The IASB requested that the staff explore for consideration at a future meeting a possible approach that would require the hedged item to be both separately identifiable and measurable for the purpose of determining hedge effectiveness.

The FASB decided to explore bifurcation-by-risk for financial items and requested the staff to develop possible approaches for consideration at a future meeting.

See the [IASB project summary](#) for more information on this project.

Financial instruments with characteristics of equity

This was not discussed at this meeting because of lack of time.

See the [IASB project summary](#) for more information on this project.

Insurance contracts

The Boards discussed reinsurance and policyholder accounting.

Reinsurance

The Boards tentatively decided that a reinsurer would measure and recognize reinsurance contracts using the same measurement and recognition methods used to measure insurance contracts.

The Boards also tentatively decided that a cedant would recognize and measure its reinsurance asset (reinsurance recoverable) using the same recognition and measurement approach that it uses for the reinsured portion of the underlying insurance contracts that it has issued. This measurement approach would include the following:

- The expected present value of the cash flows required to fulfill the reinsured portion of the insurer's obligations
- The addition of the risk margin (but not the residual margin) included in the measurement of the reinsured portion of the contract liability
- The addition of the residual margin implied by the pricing of the reinsurance contract
- The impact on the reinsurance asset of possible impairment and coverage disputes, measured using the building block approach, rather than an incurred loss basis

The Board noted that this tentative decision could change as a result of additional staff research.

In addition, the Boards also reached tentative decisions on offsetting of reinsurance balances by a cedant, derecognition of related direct insurance liabilities by a cedant on entering into a reinsurance contract, and the recognition of ceding commissions for proportional reinsurance contracts by the reinsurer and cedant.

Policyholder accounting

The Boards tentatively decided to not discuss the following issues any further before an exposure draft:

- Any differences in measurement that might arise if the Boards' proposals for insurers were applied to policyholders, except in relation to acquisition costs and participating features
- Non-reinsurance policyholder accounting

Next steps

The Boards continued their discussion of this project at the joint Board meeting on February 16-18, 2010. The results of that meeting are summarized below.

See the [IASB project summary](#) for more information on this project.

Leases

In the Discussion Paper, *Leases: Preliminary Views*, the Boards did not reach a converged definition of a lease. At that time, the Boards' preliminary view was that the scope of a proposed new standard would be based on the scope of the existing standards. The Boards recognized that differences between the standards would have to be reconciled before a new standard is issued. At this meeting, the Boards discussed this issue and tentatively decided:

- To define a lease broadly; therefore, the definition is not limited to leases of property, plant, and equipment as it is under current U.S. GAAP. However, the Boards also tentatively decided that the proposed new lease requirements would not apply to assets other than property, plant and equipment. Consequently, the overall definition of a lease would be broader than the scope of the proposed standard.
- To define a lease as a type of contract instead of an agreement to be consistent with the terminology used in the revenue recognition and insurance projects
- That the definition would state a lease is for a period of time

- That the definition would state the lessor must convey the right to use an asset. The Boards tentatively decided that the right to use an asset would be conveyed if either of the following conditions exist:
 - The contract conveys the right to use a specified asset. Additional guidance about what constitutes a specified asset will be provided to differentiate between the right to use an asset and a service or supply contract.
 - The contract conveys the right to control the use of the underlying asset. The guidance regarding when a lease conveys the right to control the use of the underlying asset in the current definition of when an arrangement contains a lease would be included in the proposed new leases requirements with revisions to clarify its meaning.
- The definition of a lease would explicitly state that there must be consideration exchanged for the right to use an asset

As a result of those tentative decisions, the Boards tentatively agreed on the following proposed definition of a *lease*:

A lease is a contract in which the right to use a specified asset is conveyed, for a period of time, in exchange for consideration.

The Boards discussed lessee and lessor accounting issues further at the February 2010 joint meeting. The results of that meeting are summarized below.

See the [IASB project summary](#) for more information on this project.

Presentation of other comprehensive income

The Boards discussed presentation of the sections of the statement of comprehensive income and the timeline for issuance of an exposure draft.

Presentation of the sections of the statement of comprehensive income

The Boards reached tentative decisions that would require

- An entity to present a continuous statement of comprehensive income showing clearly and separately profit or loss (or net income) and other comprehensive income. An entity reporting comprehensive income would be permitted to use different titles for those sections on condition that the meaning is clear.
- The components of each section of the statement to be reported consistently

The Boards also affirmed the following:

- To retain existing requirements that provide the option to display components of other comprehensive income either:
 - Net of related income tax expense; or
 - Before related income tax effects, with one amount shown for the aggregate income tax effects on the face of the continuous statement of comprehensive income and the income tax effect related to each component, including reclassification adjustments, in the notes to the financial statements
- Not to change the requirements in other standards as to which items would be required to be presented in other comprehensive income

The FASB affirmed that reclassification adjustments between other comprehensive income and profit or loss would be displayed in the same level of detail as when the items were originally reported.

The IASB affirmed that components of other comprehensive income that are not reclassified as adjustments upon derecognition and components that are reclassified as adjustments (recycled) would be presented separately.

Timeline for issuing an exposure draft

The Boards reached a tentative decision that the exposure draft would be issued simultaneously with the FASB's proposed update on financial instruments and the IASB's exposure draft on post-employment benefits in March 2010.

A [new presentation of other comprehensive income project page](#) is now available.

IASB issues February 2010 IASB meeting highlights

Key issues

At the February 2010 IASB meeting the following issues were discussed:

- *Consolidation*: the IASB tentatively decided that the disclosure requirements for subsidiaries, joint ventures, and associates would be combined within a comprehensive disclosure standard that would address a reporting entity's involvement with other entities when that involvement is not within the scope of IAS 39 or IFRS 9
- *Derecognition*: the IASB reached tentative decisions on application guidance for transfers, the meaning of economic benefits, and an exception to the derecognition criteria for repurchase agreements. The IASB also discussed unit-linked insurance, securitization vehicles, and pass-through arrangements, but did not make any decisions.
- *Joint ventures*: the IASB reached tentative decisions on a modification to

the scope paragraph of the Exposure Draft and on the use of the term *significant economic event*. The IASB plans to issue the final IFRS at the end of the second quarter of 2010.

- *Post-employment benefits*: the IASB tentatively approved a revised set of disclosures for the exposure draft forthcoming in March 2010
- *Rate regulated activities*: the staff was asked to perform additional research and analysis on this project with a focus on whether regulatory balances qualify as assets and liabilities in accordance with the current Framework and are consistent with other IFRS

All decisions reached at IASB meetings are tentative and may be changed or modified at future meetings. Board decisions become final only after completion of a formal ballot to issue a Standard or Interpretation or to publish an Exposure Draft.

The International Accounting Standards Board has issued an [IASB Update](#), which summarizes the IASB meeting that was held in London on February 15-19, 2010.

Highlights of the meeting are discussed below.

Consolidation

At this meeting, the IASB discussed whether the proposed disclosures in ED 10, *Consolidated Financial Statements*, and ED 9, *Joint Arrangements*, as well as the disclosures in IAS 28, *Investments in Associates*, should be combined into a comprehensive disclosure standard to address a reporting entity's involvement with other entities that are outside the scope of IAS 39, *Financial Instruments: Recognition and Measurement*, and IFRS 9, *Financial Instruments*. The IASB also discussed the disclosure of information about a reporting entity's exposure to risk from structured entities that the reporting entity does not control.

The IASB tentatively decided that the disclosure requirements for subsidiaries, joint ventures, and associates would be combined within a comprehensive disclosure standard that would address a reporting entity's involvement with other entities when that involvement is not within the scope of IAS 39 or IFRS 9. The IASB also tentatively decided that the disclosure standard would include the disclosure requirements for joint operations even though the joint operations might not be related to involvement with another entity. A joint operation is classified as a type of joint arrangement in ED 9.

In addition, the IASB tentatively decided that a reporting entity would disclose information that enables users of its financial statements to evaluate the nature of, and risks associated with, the reporting entity's involvement with structured entities that the reporting entity does not control within a comprehensive disclosure standard for a reporting entity's involvement with other entities.

See the [IASB project summary](#) for more information on this project.

Derecognition

The IASB continued its deliberations of the feedback received on the Derecognition Exposure Draft published in March 2009. The IASB has tentatively decided to adopt a derecognition approach that requires an entity to derecognize a financial asset when the economic benefits inherent in that asset no longer exist or when the benefits exist but the entity ceases to have the present ability (a) to obtain all of those benefits or (b) to restrict others' access to them.

At this meeting, the IASB made the following tentative decisions:

- The next due process document for derecognition of financial instruments will not provide a definition of *transfer*, but will provide application guidance to address the concerns raised by respondents to the Exposure Draft with respect to that definition. The concerns were generally in regard to whether and when a transfer had occurred in various circumstances.
- The term *economic benefits*, as that term is used in the proposed derecognition approach, encompasses the economic benefits associated with both the financial and nonfinancial components of a contract within the scope of IAS 39, provided that the economic benefits associated with the nonfinancial component of the contract have not been recognized separately. Nonfinancial rights would include items such as voting or subscription rights. If an entity were to sell the nonfinancial right (and the associated economic benefits), it would derecognize the entire financial asset and then recognize a new asset for the right to the economic benefits from the financial component.
- To make an exception to the derecognition criteria as they apply to sale and repurchase agreements and similar transactions. The exception requires that any sale of a financial asset that is accompanied by an agreement that entitles and obligates the entity to repurchase the asset before maturity of the asset should be accounted for as a secured borrowing (similar to the accounting for such transactions under FASB Statement 166, *Accounting for Transfers of Financial Assets - an amendment of FASB Statement No. 140*). The IASB would seek to align the exception, to the extent feasible, with the “effective control” guidance under FASB Statement 166. Effective control over the transferred assets is maintained if the agreement both entitles and obligates the transferor to repurchase or

redeem transferred financial assets from the transferee and additional specific conditions are met.

The IASB also discussed the application of the derecognition approach to unit-linked insurance products, securitization vehicles, and pass-through arrangements. No decisions were made.

The IASB will continue its deliberations on the proposed derecognition approach at future meetings.

See the [IASB project summary](#) for more information on this project.

Joint ventures

The IASB continued its deliberations on the proposals in its Exposure Draft, *Joint Arrangements*.

Scope

The IASB tentatively decided to modify the scope paragraph of the Exposure Draft to include all entities when accounting for interests in joint arrangements. The current exemption in IAS 31, *Interests in Joint Ventures* for venture capital organizations, mutual funds, unit trusts, and similar entities including investment-linked insurance funds will be removed. The scope paragraph in IAS 28, *Investments in Associates* will be modified to align with this tentative decision.

Loss of joint control

The IASB tentatively decided to use the term *significant economic event* only in reference to loss of control and not loss of joint control or significant influence.

In addition, the IASB tentatively decided to:

- Confirm that the proposed requirements in the Exposure Draft for the loss of joint control would be included in the final standard
- Amend IAS 21, *The Effects of Changes in Foreign Exchange Rates* to treat a loss of joint control over a joint venture that includes a foreign operation where the investor retains significant influence as a partial disposal

The IASB will continue its deliberation of this project at a future meeting and plans to issue the final IFRS at the end of the second quarter of 2010.

See the [IASB project summary](#) for more information on this project.

Post-employment benefits

The IASB tentatively approved a revised set of disclosures (included in the February 2010 Agenda paper 12) for the forthcoming exposure draft to amend IAS 19, *Employee Benefits*. In addition, the IASB tentatively decided that it would exempt plan assets from the scope of the forthcoming standard on fair value measurements.

The IASB plans to issue the exposure draft on post-employment benefits in March 2010.

See the [IASB project summary](#) for more information on this project.

Rate regulated activities

The IASB began its discussions on the comment letters received on the Exposure Draft, *Rate-regulated Activities*, issued in July 2009. The Board discussed the background on the issue, summaries of the comments received, and the main technical issues.

The IASB did not make any tentative decisions on specific aspects of the project, except to tentatively finalize the transition relief for first-time adopters.

The transition relief is expected to be included in the omnibus *Improvements to IFRSs* due to be issued in April 2010.

The IASB asked the staff to perform additional research and analysis on this project with a focus on whether regulatory balances qualify as assets and liabilities in accordance with the current *Framework for the Preparation and Presentation of Financial Statements* and are consistent with other IFRS.

The IASB will continue its deliberation of this project at a future meeting.

See the [IASB project summary](#) for more information on this project.

IASB issues February 2010 joint IASB/FASB meeting highlights

Key issues

At its February 2010 joint meeting the following issues were discussed:

- *Consolidation*: the Boards reached a tentative decision that an investment company would not have to consolidate investments in entities that it controls. Instead, these investments would be measured at fair value.
- *Fair value measurement*: the Boards reached tentative decisions on highest and best use of nonfinancial assets, incremental value, valuation premise for nonfinancial assets, measuring financial instruments, premiums and discounts, and measuring difficult to value assets and liabilities. The IASB tentatively decided not to provide a practical expedient for valuing investments in investment companies.
- *Financial instruments – classification and measurement*: the IASB made tentative decisions on measurement and bifurcation of financial liabilities that are held for contractual cash flows and that have “vanilla” cash flow

characteristics; on bifurcation of financial liabilities that are held for contractual cash flows and that have “non-vanilla” cash flow characteristics; and on the fair value option

- *Financial instruments – hedge accounting*: the Boards discussed criteria for hedged risks designation and bifurcation-by-risk approaches for hedged financial items. The IASB tentatively decided to explore a new criterion for determining eligible risk components. The FASB tentatively decided to permit bifurcation-by-risk and to continue to discuss identification of hedged risk and assessment of risk effectiveness.
- *Financial instruments with characteristics of equity*: the Boards reaffirmed all their previous decisions in the project, and made further decisions regarding equity instruments, convertible debt, puttable shares, freestanding written put options, and classification of subsidiary instruments in consolidated financial statements
- *Financial statements presentation*: the Boards reached tentative decisions on application guidance for analysis of changes in significant asset and liability line items, definition of a remeasurement, new categories for financing arising from operating activities and for assets and liabilities arising from equity, statement of cash flows for financial service entities, and divergence issues. The Boards plan to issue the exposure draft by the end of April 2010 with a five-month comment period.
- *Insurance contracts*: the Boards reached tentative decisions on presentation of the performance statement and unit linked contracts
- *Leases*: a contract would be considered a purchase or sale, and therefore would be excluded from the proposed new lease requirements, if at the end of the contract, the contract transfers control of the underlying asset or all but a trivial amount of the risks and benefits associated with the

underlying asset

- *Revenue recognition*: the Boards tentatively decided that
 - The scope of the proposed model would exclude accounting for contracts with customers that are covered by other standards, such as lease contracts, insurance contracts, guarantees, and financial instruments
 - An entity would apply the proposed revenue recognition standard on a full retrospective basis
- *Right of offset*: the Boards held a joint education session on the netting provisions in ISDA Master Agreements. No decisions were made.

All decisions reached at IASB meetings are tentative and may be changed or modified at future meetings. Board decisions become final only after completion of a formal ballot to issue a Standard or Interpretation or to publish an Exposure Draft.

The International Accounting Standards Board has issued an [IASB Update](#), which summarizes the joint IASB/FASB meeting that was held in London on February 16-19, 2010, with the FASB participating via video conference.

Highlights of the joint meeting are discussed below.

Consolidation

IAS 27, *Consolidated and Separate Financial Statements*, requires all reporting entities, including investment companies, to consolidate entities that they control. ED 10, *Consolidated Financial Statements*, proposed to retain that scope. U.S. GAAP and some other national standard setters provide exceptions for investment companies that measure investments in entities they control at fair value. To address this difference and other concerns of respondents to ED 10, the Boards discussed whether investments that are controlled by an entity

that is considered an investment company should be consolidated or measured at fair value and not consolidated.

The Boards tentatively decided to not require investment companies to consolidate investments in entities they control. Instead, investment companies would be required to measure investments in entities they control at fair value. To ensure that the Board's tentative decision would be applied appropriately, the Boards discussed how to define an investment company. The Boards tentatively decided that the guidance in FASB ASC Topic 946, *Financial Services – Investment Companies*, would be used as the basis to develop the criteria of an investment company. The staff was instructed to work on removing U.S. specific references and to address other implementation concerns about the guidance in Topic 946.

In addition, the Boards tentatively decided that additional disclosures would be required about entities that an investment company controls when it measures investments in those entities at fair value. The disclosures will be developed as part of the new disclosure requirements for involvement with controlled entities.

See the [IASB project summary](#) for more information on this project.

Fair value measurement

The Boards discussed the following topics:

- Highest and best use of nonfinancial assets
- Incremental value
- Valuation premise for nonfinancial assets
- Measuring the fair value of financial instruments
- Premiums and discounts in a fair value measurement

- Measuring the fair value of difficult to value assets and liabilities (including unquoted equity instruments)
- Measuring the fair value of investments in investment company entities

Highest and best use of nonfinancial assets

The Boards addressed whether a fair value measurement should consider a nonfinancial asset's highest and best use. Highest and best use refers to the use of the asset, or group of assets within which the asset would be used, by market participants in a way that would maximize the asset's value. Assuming rationality on the part of market participants, an observed market price should reflect the highest and best use of an asset.

The IASB's exposure draft had clarified the meaning of *physically possible*, *legally permissible*, and *financially feasible* in the context of highest and best use. For example, in determining the highest and best use of a parcel of land, physically possible would consider location or size; legally permissible would consider applicable zoning regulations; and financially feasible would consider whether the investment is expected to provide adequate returns. Some comment letters had asked for further clarification for those three terms.

The Boards tentatively decided:

- That a fair value measurement of a nonfinancial asset considers its highest and best use by market participants
- To describe the meaning of the terms physically possible, legally permissible, and financially feasible

Incremental value

An entity may be using an asset together with other assets in a manner that differs from the asset's highest and best use. For example, an entity might operate a factory on a parcel of land even though the highest and best use of

the land would be to demolish the factory and build residential property. The difference between the current use and the highest and best use is referred to as the incremental value. The Boards considered whether to require entities to separate the fair value of the asset group into two components, current use and incremental value, to arrive at a fair value measurement, or to just provide relevant disclosure.

The Boards tentatively decided:

- Not to require entities to separate the fair value of an asset group into two components when an entity uses an asset in a way that differs from its highest and best use
- To require entities to disclose information about when they use an asset in a way that differs from its highest and best use (and that asset is recognized at fair value based on its highest and best use)

Valuation premise for nonfinancial assets

The highest and best use of an asset establishes the valuation premise, which can be either in-use or in-exchange. The valuation premise is in-use if the asset would provide maximum value to market participants principally through its use in combination with other assets and liabilities as a group (as installed or otherwise configured for use). The valuation premise is in-exchange if the asset would provide maximum value to market participants principally on a stand-alone basis.

The in-use valuation premise assumes market participants will use the asset in combination with other assets and liabilities that are available to the market participants. These are referred to as “complementary assets” and “complementary liabilities.” In other words, the market participants are assumed to have the rest of the assets in the asset group, but are lacking this particular asset. For example, a pipe with a machine at each end is not suitable

for any other purpose than to connect the machines. Without the assumption that the market participant has the machines, the pipe would only have scrap value. The in-use valuation premise would assume the presence of the two machines for purposes of determining the fair value of the pipe.

Some comment letters expressed confusion regarding the terms in-use and in-exchange. However, those terms are common in practice and are included in FASB ASC Topic 820, *Fair Value Measurements and Disclosures* in the U.S. The Boards discussed whether to provide further explanation of the meaning of the terms or to remove the terms from the standard and describe the objective instead.

The Boards tentatively decided:

- That the objective of a fair value measurement of an individual asset is to determine the price for a sale of that asset alone, not for a sale of that asset as part of a group of assets or business. However, when the highest and best use of an asset is to be used as part of a group of assets, the fair value measurement of that asset presumes that the sale is to a market participant that has, or can obtain, the "complementary assets" and "complementary liabilities." Complementary liabilities include working capital but do not include financing liabilities.
- To describe the objective of the valuation premise without using the terms in-use and in exchange because those terms are often misunderstood

Measuring the fair value of financial instruments

The Boards considered whether the concept of highest and best use would apply to financial assets and to liabilities. Some believe that financial assets have alternative uses because they can be combined with other instruments in

a portfolio or otherwise modified, as when packaged for securitization. Others believe that combining financial assets within a portfolio is not a different use, and otherwise changing the terms of a financial asset results in a different financial asset. Some believe that liabilities have alternative uses because liabilities may be discharged in different ways, such as fulfillment, extinguishment, or transfer. Others believe that the manner of settling a liability does not represent an alternative use.

Because the highest and best use determines the valuation premise, if the concept of highest and best use does not apply there would be no valuation premise to apply. If the Boards were to decide that highest and best use does not apply to financial assets and to liabilities, then the valuation premise becomes irrelevant.

When there is not a quoted price for the fair value of a financial instrument, an entity using valuation techniques might need to make valuation adjustments when the model used does not properly estimate the price at which an orderly transaction would take place between market participants on the measurement date. For example, an entity might make adjustments related to model calibration, liquidity, credit risk, complexity, and other risk adjustments. Consistent with the objective of fair value measurement, an entity would only include those adjustments that market participants would make under current market conditions.

The Boards considered whether to provide a practical expedient to measure the fair value of a financial asset or a financial liability by considering offsetting risk positions within a portfolio. The fair value measurement would not be applied to each of the individual instruments, but to the offsetting position, which is comprised of a group of instruments. It would be market based in the sense

that it considers what a market participant would consider in determining a price it is willing to pay for the same net risk exposure.

The Boards tentatively decided:

- That the concepts of highest and best use and of valuation premise are relevant only for nonfinancial assets and not relevant for financial assets or for liabilities
- To describe valuation adjustments that entities might need to make when using a valuation technique to reflect the adjustments that market participants would make to price a financial instrument under the market conditions at the measurement date. These valuation adjustments were described in the IASB's Expert Advisory Panel report, *Measuring and Disclosing the Fair Value of Financial Instruments in Markets That Are No Longer Active*.

The Boards will discuss at a future meeting whether the fair value of financial instruments within a portfolio should consider offsetting risk positions, including credit risk and market risk.

Premiums and discounts in a fair value measurement

A blockage factor is an estimate of the reduction in the quoted price of a financial instrument (especially equities) that would occur if a market participant were to sell a large holding of instruments at once. Many view the investment as the holding of the instruments, not the individual share, so they believe that a blockage discount is appropriate. Others view the blockage discount as specific to the transaction, rather than the financial instrument, and therefore would not be considered in a fair value measurement. Whether the blockage discount occurs is a function of how the entity sells the shares – all at once or in smaller batches.

There are other premiums and discounts that market participants would consider in pricing an asset or liability. A control premium is the additional price a market participant would pay to obtain a controlling interest in another entity. A minority interest discount reflects the fact that minority shareholders do not have the same rights as the controlling shareholder. A discount for lack of marketability, which is different than a blockage discount as it applies to any size holding, reflects the inability of a market participant to convert an asset into a predictable amount of cash quickly and at reasonably low cost.

The Boards tentatively decided:

- To clarify what a blockage factor is and to describe how it is different from other types of adjustments, such as a discount for lack of marketability, to an individual instrument
- To prohibit the application of a blockage factor at any level of the fair value hierarchy
- To specify that a fair value measurement in Levels 2 and 3 of the fair value hierarchy considers other premiums and discounts that market participants would consider in pricing an asset or liability at the unit of account specified in the relevant standard (except for a blockage factor)

Measuring the fair value of difficult to value assets and liabilities (including unquoted equity instruments)

The Boards considered how much guidance to provide regarding the valuation of difficult to value assets and liabilities. General information on valuation techniques and how to select inputs to those techniques would be useful, however at some point, additional guidance becomes inconsistent with a principles-based standard. While some would prefer guidance on how to value unquoted equity instruments, it would be difficult to not also provide guidance

on other assets and liabilities, which would be neither principles-based nor practical.

Guidance on when cost might be an appropriate estimate of fair value has been provided previously in other standards (e.g. IFRS 9, *Financial Instruments* and IAS 16, *Property, Plant and Equipment*). The Boards considered whether such guidance should remain in individual standards or be included in a converged fair value measurement standard. As such guidance is specific to the particular assets and liabilities it would be difficult to develop specific guidance that is appropriate for all types of assets and liabilities.

The Boards tentatively decided:

- Not to include additional guidance for measuring the fair value of difficult to value assets and liabilities (including unquoted equity instruments). At a future meeting, the IASB will discuss the need for developing educational materials to assist entities with applying the fair value measurement guidance to such assets and liabilities.
- Not to include indicators of when cost might be an appropriate estimate of fair value

Measuring the fair value of investments in investment company entities

The IASB discussed whether to provide a practical expedient allowing entities with investments in investment company entities to use reported net asset value without adjustment as a measure of fair value in specific circumstances (e.g. when there are restrictions on redemption). Such a practical expedient is included in FASB ASC Topic 820, *Fair Value Measurements and Disclosures*, provided that the underlying investments of the investment company are measured at fair value and the net asset value is determined as of the reporting entity's measurement date.

The Board tentatively decided not to provide such a practical expedient because IFRS do not have accounting requirements that are specific to investment company entities and it would be difficult to prescribe the circumstances in which it could be applied given the different practices for calculating net asset values in jurisdictions around the world.

See the [IASB project summary](#) for more information on this project.

Financial instruments: classification and measurement

Both Boards were present for the discussions; however, only the IASB was asked to make any decisions.

The tentative decisions described below, coupled with the tentative decisions made at the February 10, 2010 meeting, described above, effectively retain the measurement requirements in IAS 39, *Financial Instruments: Recognition and Measurement* for financial liabilities, except for the proposed changes to the fair value option. The IASB's tentative decisions about financial liabilities respond to issues raised about recognizing gains or losses arising from changes in an entity's own credit risk.

Amortized cost measurement

As described above, the staff grouped financial liabilities into three broad categories. The third category, instruments that are held to pay contractual cash flows and have “vanilla” contractual cash flow characteristics, was discussed at this meeting. When previously exposed, amortized cost treatment for this category of financial instruments received wide support. At this meeting, the IASB tentatively decided that financial liabilities would be measured at amortized cost if they are not held for trading, and if they do not have embedded derivative features that would require bifurcation under IAS 39.

Bifurcation

At a previous meeting, the IASB tentatively decided to bifurcate financial liabilities that are held to pay contractual cash flows, and that have “non-vanilla” contractual cash flow characteristics. At this meeting, the Board considered whether to use a bifurcation approach that is based on the classification conditions in IFRS 9, *Financial Instruments*, where bifurcation would be based on the liability’s contractual cash flow characteristics. Under that approach, an instrument would be bifurcated if the host component had cash flow characteristics that are solely payments of principal and interest on the principal amount outstanding, with the host measured at amortized cost and the other component or components measured at fair value through profit or loss. There were concerns that this approach could increase complexity, and would require application guidance for certain liability instruments that would not need to be separated under existing guidance.

As a result, the Board tentatively decided that the bifurcation requirements in IAS 39 should be retained. An embedded derivative would be separated from the host contract if certain conditions were met. The derivative is measured at fair value while the host is measured at amortized cost, unless the fair value option is elected. Constituents report that, unlike for assets, current guidance for liabilities appears to be working well.

Fair value option

The IASB tentatively decided to retain the fair value option (FVO) and carry forward the three eligibility conditions in IAS 39 (accounting mismatch, managed on a fair value basis, and contains an embedded derivative).

In response to issues raised, the Board discussed how to recognize gains or losses arising from changes in an entity's own credit risk. The staff had

recommended a hybrid approach that called for the liability to be reflected at full fair value on the balance sheet, with the total fair value change recognized in profit or loss, and the portion attributable to the change in own credit risk recognized in equity with an offsetting entry to profit or loss. The advantage to this approach would be that the relevant information would be presented on the face of the income statement, but the change in own credit risk would not affect profit or loss. This hybrid approach, which would not expand the use of other comprehensive income (OCI), reflects the notion that a change in the credit risk of an entity's liabilities represents a transfer of wealth between the liability holders and the equity holders.

Some disadvantages to the proposed hybrid approach were noted. Recognizing the change directly in equity raises the question of whether that approach should be used for other items. Equity changes, other than net income or loss, are supposed to represent transactions between an entity and its owners. OCI is an accepted place for items that affect performance, and recycling items out of equity (if necessary) would be unusual. Also, there may be jurisdictions where these items would not constitute equity.

The IASB tentatively decided that for all financial liabilities measured at fair value under the FVO, an entity would be required to:

- Recognize the total fair value change in profit or loss
- Recognize the portion attributable to changes in own credit risk in OCI (with an offsetting entry to profit or loss)

Amounts recognized in OCI would not recycle into profit or loss

See the [IASB project summary](#) for more information on this project.

Financial instruments: hedge accounting

The Boards discussed possible criteria for designation of eligible hedged risks and possible bifurcation-by-risk approaches for hedged financial items. Although both Boards were receptive to bifurcation-by-risk approaches, it is difficult to specify hedge accounting models while the Boards have different models for classification and measurement of financial instruments.

The IASB had expressed concern that a broad approach to designating risk components as eligible hedged items (bifurcation-by-risk) would mean a free choice in componentization that could automatically lead to 100% effectiveness. The staff noted that empirical evidence from the application of IAS 39 to financial hedged items had concluded that not all risk components are eligible for hedge accounting and those that are eligible do not automatically result in perfect effectiveness when hedged. However, the staff believed that the current guidance is rule-based and internally inconsistent and recommended not carrying forward the existing requirements. As a result, the IASB tentatively decided to explore a new criterion for the purpose of determining risk components eligible for designation as hedged items.

The FASB tentatively decided that bifurcation-by-risk would be permitted for hedged financial items within the context of the recognition and measurement model agreed to by the Board for accounting for financial instruments. The Board will continue to discuss issues relating to hedge accounting, specifically how to identify the hedged risk and how the assessment of effectiveness will be determined.

See the [IASB project summary](#) for more information on this project.

Financial instruments with characteristics of equity

The Boards reaffirmed their previous classification decisions:

- Instruments currently accounted for under the share-based payment literature are not within the scope of this project
- The following types of instruments would be equity in their entirety:
 - Perpetual instruments (instruments not required to be redeemed except for forced liquidation or by choice) issued by entities without specified limits to their lives (including both ordinary and preferred shares)
 - Mandatorily redeemable and puttable instruments that meet either of the following criteria:
 - The instrument's terms require or permit redemption to allow an existing group of shareholders, partners, or other participants to maintain control of the entity when one of them chooses to withdraw
 - The holder must own the instrument in order to engage in transactions with the entity or otherwise participate in the activities of the entity, and the instrument's terms require or permit redemption when the holder ceases to engage in transactions or otherwise participate
- All other mandatorily redeemable instruments (instruments that must be redeemed on a certain date or on the occurrence of an event that is certain to occur) would be classified as liabilities
- Contracts that require or may require an entity to issue a specified number of its own perpetual equity instruments in exchange for a specified price (including call options, forward contracts to issue shares, rights issues, and purchase warrants) would be classified as equity. The specified number

must be either fixed or vary only so that the counterparty will receive a specified percentage of total shares that were outstanding on the issuance date for a specified price. The specified price must be fixed in the reporting entity's currency or, in some cases, in the currency of the shareholder.

- Instruments that require an entity to issue a specified number of its own perpetual equity instruments for no additional compensation would be classified as equity (for example, prepaid forward contracts to issue shares)
- The entity's ability to issue its own perpetual equity instruments to settle share-settled instruments classified as equity would be assessed at the date that each instrument is issued and at each reporting date thereafter. If, at any time, the entity does not have enough authorized shares to settle a share-settled instrument classified as equity, that instrument would be reclassified as a liability and left there for the remainder of its life.
- Preferred shares that must be converted into a specified number of common shares on a specified date or on the occurrence of an event that is certain to occur would be classified as equity
- Contracts that require an entity to repurchase its own shares on a specified date or on the occurrence of an event that is certain to occur would be separated into a liability representing the amount to be paid (measured according to standards for similar freestanding instruments) and an offsetting debit to equity (grossed up)

Equity instruments

The Boards decided that the following types of instruments would be classified as equity:

- A nominally perpetual instrument issued by a limited-life entity or that must be liquidated at the option of an instrument holder. That means an instrument that would otherwise be equity will not become a liability merely because it is issued by an entity that is not or may not be able to continue to exist indefinitely.
- A contract that requires an entity to issue for a specified price (or for no future consideration) a specified number of puttable or mandatorily redeemable instruments that will be equity in their entirety when issued. Examples include a forward contract to issue mandatorily redeemable equity instruments and an identical forward contract that has been prepaid.
- A contract that requires the entity to issue for a specified price (or for no future consideration) a specified number of derivatives that will require the entity to issue a specified number of instruments that will be equity in their entirety when issued. Examples include a forward contract to issue a written call option on the entity's own shares and an identical forward contract that has been prepaid.
- Preferred shares that must be converted into a specified number of perpetual equity instruments
- Preferred shares that must be converted into a specified number of puttable or mandatorily redeemable instruments that will be equity in their entirety when issued

Convertible debt

The Boards decided that a bond (or other debt instrument) would be separated into a liability component and an equity component provided that it is convertible at the option of the holder into a specified number of instruments that will be equity in their entirety when issued. All other convertible debt instruments would be classified as liabilities in their entirety.

Puttable shares (redeemable at the option of the holder)

Puttable shares that are not classified as equity in their entirety should be separated into liability and equity components. The liability component, which represents a written put option, should be accounted for as a freestanding written put option.

Presentation of freestanding written put options

A freestanding written put option would be presented net as a liability in its entirety.

Classification of subsidiary instruments in consolidated financial statements

Instruments classified as equity in a subsidiary's financial statements would be classified as equity in consolidated financial statements unless the nature of the instrument changes in consolidation because of arrangements between the instrument holder and another member of the consolidated group. If the nature of the instrument changes in consolidation, classification would be reconsidered in the consolidated financial statements.

See the [IASB project summary](#) for more information on this project.

Financial statement presentation

The Boards continued discussions of the proposals in the Discussion Paper, *Preliminary Views on Financial Statement Presentation*, specifically addressing:

- Application guidance for analysis of changes in significant asset and liability line items
- Definition of a remeasurement and related guidance
- New categories for “financing arising from operating activities” and for “assets and liabilities arising from equity”
- Statement of cash flows for financial service entities
- Divergence issues

- Sweep issues
- Support for package of decisions

Application guidance for analysis of changes in significant asset and liability line items

The Boards discussed several implementation issues with respect to the tentative decision reached in October 2009 to require an entity to present in the notes to the financial statements an analysis of changes in the balances of all significant asset and liability line items.

At the February 2010 joint meeting, the Boards reached a tentative decision that the exposure draft would

- Permit an entity to present each analysis of changes with related information in a topic specific note disclosure. For example, an analysis of changes in an entity's property, plant and equipment line items could be presented as part of the entity's property, plant and equipment note. In all cases, each analysis must be accompanied by a narrative explanation of the changes.
- Require each analysis of changes reported in the current reporting period to include a comparative analysis of changes for the prior reporting period(s)
- Clarify that an entity would always disclose reconciliations of specific items as required elsewhere in IFRS or U.S. GAAP, notwithstanding the factors to be considered in determining whether the change in an asset or liability would be analyzed in the notes
- Clarify that, when preparing a reconciliation of specific items as required elsewhere in IFRS or U.S. GAAP, an entity would consider whether the reconciliation reflects the required components that are part of the analysis of changes

- Clarify that an entity would provide disaggregated information for each component of an analysis of changes. For example, an entity cannot aggregate items that meet the definition of a remeasurement into one line item.

Definition of a remeasurement and related guidance

At the joint meeting in October 2009, the FASB tentatively agreed to require disaggregation of remeasurements on the statement of comprehensive income in a columnar format. The IASB expressed a preference for presenting information about remeasurements in the notes to financial statements. Both Boards seem to agree that providing this type of information could help users understand and assess an entity's performance, but there was a lack of consensus on what exactly to disaggregate as a remeasurement. Both Boards also agreed that the notes to financial statements would include a description or explanation of the remeasurement information presented on the statement of comprehensive income/in the notes. If that explanation accompanies the related analyses of change in the balance of the item, it would not have to be repeated elsewhere in the notes.

At the February 11, 2010 joint meeting, the Boards reached a tentative decision that a *remeasurement* would be defined as “an amount recognized in comprehensive income that reflects the effects of a change in the net carrying amount of an asset or liability, and that is the result of:

- A change in (or transacting at) a current price or value
- A change in an estimate of a current price or value; or
- A change in any estimate or method used to measure the carrying amount of an asset or liability”

The Boards tentatively decided that the sale of ordinary inventory (including the realized income from the market-making activities of broker-dealers)

would not be presented as a remeasurement. Although the sale of ordinary inventory at an amount different than carrying amount would, in principle, reflect a remeasurement, these remeasurements are fundamentally different in character than other types of realized remeasurements (e.g. the sale of PP&E). Whereas most realized remeasurements reflect a correction of previously estimated values (e.g. having previously taken too much or too little depreciation relative to the amount of consideration realized on disposition), the realized *remeasurement* that occurs when inventory is sold reflects the (previously unrecognized) gross margin from an entity's major operations. The staff provided examples of items that would be presented as a remeasurement and those that would not be presented as a remeasurement.

New categories for “financing arising from operating activities” and for “assets and liabilities arising from equity”

Financing arising from operating activities

In December 2009, the Boards reached a tentative decision to add a new category to the business sections of the statements of financial position and comprehensive income, which would be labeled “financing arising from operating activities.”

At their February 2010 joint meeting, the Boards reached a revised tentative decision that financing arising from operating activities would be included in a new subcategory in the operating category of the statements of financial position and comprehensive income rather than in a separate category in the business section. The cash flows related to these items would be presented in the operating category in the statement of cash flows. Accordingly, the statement of cash flows would not include the new subcategory. The Boards clarified that the new subcategory would include all liabilities (and assets bound to the related obligation for the purpose of settling the liability) that

- Do not meet the definition of *financing*
- Are initially long term
- Have a time value of money component that is evidenced either by interest or an accretion of the liability because of the passage of time
- Examples of items that would be included in the subcategory of financing arising from operating activities include:
- A net pension obligation (or asset)
- Lease obligations
- Asset retirement obligations
- Vendor financing (that is, a long-term payable that relates to a supplier providing a specific good used in production or providing a specific service)
- Deferred compensation arrangements other than share-based payments (and any associated asset), such as a bonus earned that is to be paid at a later date
- Structured settlements (for example a worker's compensation claim that has been settled and will be paid out over a period of time)
- Contingencies that are discounted pursuant to IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*

Assets and liabilities arising from equity

In October 2009, the Boards reached a tentative decision that the *debt category* would include liabilities where the nature of those liabilities is a borrowing arrangement entered into for the purpose of raising capital. That borrowing arrangement is usually transacted on an arm's-length basis on market terms. At the February 2010 meeting the Boards tentatively decided that the debt category would include a new subcategory “assets and liabilities arising from

equity” (e.g. a dividend payable, a written put option on an entity's own shares, or a prepaid forward purchase contract for an entity's own shares). The Boards clarified that assets and liabilities that arise from transactions involving an entity's own equity would be presented separately from borrowing arrangements within the debt category.

Statement of cash flows for financial service entities

At their respective Board meetings in January 2010, the FASB and the IASB considered how a financial services entity should present cash flow information in the statement of cash flows. At the joint meeting in February 2010, the Boards tentatively decided that the exposure draft would

- Require the presentation of cash flows for loans made to customers and principal collections of loans on a gross basis. However, the existing requirements about the types of cash flows that may be reported net on a statement of cash flows would be retained (see IAS 7, *Statement of Cash Flows* and FASB ASC Topic 230, *Statement of Cash Flows*).
- Require the direct method statement of cash flows
- Require an entity with funds held on deposit to present cash inflows and outflows so that its statement of cash flows reflects transactions between the entity and its depositors as if they were settled by external funds

The Boards also reached a tentative decision to specifically ask respondents to the exposure draft for input on the costs and benefits of presenting cash flows with respect to the above tentative decisions.

Divergence issues

The Boards discussed the issues on which they have reached different tentative decisions to date with respect to financial statement presentation issues.

Resolution of FASB divergence issues

- *Exposure draft*: the FASB affirmed that its exposure draft would
 - Not include a requirement to disclose net debt information in the notes to financial statements
 - Not include minimum line item requirements for the statement of financial position
- *Segment disclosures*: the FASB reaffirmed its decisions to
 - Require disclosure of operating assets, liabilities, and cash flows by reportable segment
 - Require an entity with more than one reportable segment to present its by-nature information in its segment note
- *Presentation of remeasurement information*: the FASB decided to change its December 2009 tentative decision to require the presentation of remeasurement information in a separate column on the statement of comprehensive income. Instead, the FASB agreed to present that information in a separate note to the financial statements. As a result, the Boards' respective exposure drafts will be the same on this issue.

Resolution of IASB divergence issues

- *Exposure draft*: the IASB affirmed that its exposure draft would
 - Require presentation of net debt information as part of the analyses of changes
 - Include minimum line item requirements for the statement of financial position
- *Segment disclosures*: the IASB reaffirmed its decisions to:

- Not include a requirement to disclose operating assets, liabilities, and cash flows by reportable segment
- Change its October 2009 tentative decision and require an entity with more than one reportable segment to present its by-nature income and expense information in a new note rather than in its segment note
- *Deferred tax assets and liabilities*: the IASB tentatively decided to retain the Discussion Paper proposal that deferred tax assets and liabilities would be classified as short term or long term according to the classification of the related asset or liability. This classification approach is consistent with U.S. GAAP.

The IASB noted that IFRS 8, *Operating Segments* is scheduled for a post-implementation review in 2011. As part of that review, the IASB committed itself to consider whether existing requirements for segment reporting should be brought into line with the amendments to FASB ASC Topic 280, *Segment Reporting* that the FASB will make as part of the financial statement presentation project.

Sweep issues

Sweep issues are those issues that have not been reconsidered by the Boards because respondents to the Discussion Paper expressed few concerns about these proposals.

The Boards tentatively decided that the exposure draft would

- Include the current requirements in IAS 1 for the statement of changes in equity
- Include the general offsetting principle from IAS 1
- Remove the proposal in the Discussion Paper that classification of items into sections and categories is an accounting policy. However, an entity

would be required to relate its presentation of assets and liabilities (and changes in those assets and liabilities) to its business.

- Retain the Discussion Paper proposal that subtotals and headings for each section and category would be presented in the financial statements. In addition, subtotals and headings would be presented for all subcategories.
- Require disaggregation of similar cash flows when the nature of the cash flow and timing of the payment in relation to its recognition in profit and loss is relevant to an understanding of the entity's change in cash for the period
- Not address disclosure of information about the maturities of contractual long-term assets and liabilities

Support for package of decisions

The staff presented a summary of the Boards' tentative decisions to date with respect to the financial statement presentation project. The agenda paper includes a high level comparison of the Discussion Paper and the main provisions that will be in the exposure draft (based on tentative decisions to date). The Boards asked the staff to draft an exposure draft for balloting.

The Boards tentatively decided that the exposure draft would have a five month comment period. The Boards plan to issue the exposure draft by the end of April 2010.

See the [IASB project summary](#) for more information on this project.

Insurance contracts

The Boards discussed:

- Accounting for insurance, investment, and service components included in an insurance contract
- Presentation of the performance statement
- Unit linked contracts

Unbundling

The Boards discussed whether the components of an insurance contract should be accounted for as a single contract or as if those components were separate contracts (unbundled), but did not reach a tentative decision. The Boards instructed the staff to further develop an approach that would not require unbundling for recognition and measurement if components are significantly interdependent.

The IASB tentatively decided that the approach for unbundling that is being developed for insurance contracts would be used to unbundle derivatives embedded in insurance contracts, subject to satisfactory completion of the work on that approach instead of the approach used for financial instruments. The FASB deferred reaching a decision until the staff develops further guidance on interdependency.

Presentation of the performance statement

The Boards tentatively decided that the measurement approach would drive the presentation model for the performance statement and that the staff should further develop an expanded margin approach.

Unit linked contracts

The Boards tentatively decided that assets and related liabilities associated with unit linked contracts, including those described as separate accounts, would be

reported as the insurer's assets and liabilities in the statement of financial position.

The Boards also tentatively decided that issues involving the consolidation of investment funds associated with unit-linked contracts (including separate account contracts) are within the scope of the consolidation project and not within the scope of the insurance contracts project.

Next steps

The Boards will discuss this project further at their meetings in March 2010.

See the [IASB project summary](#) for more information on this project.

Leases

The Boards discussed:

- Accounting for changes in contingent rentals
- Determining when contracts are purchases or sales of the underlying asset
- Defining initial direct costs
- Defining the interest rate implicit in the lease
- Transitional provisions for lessees

Accounting for changes in contingent rentals

At a prior meeting, the Boards had tentatively decided that the lessee's obligation to pay rentals and the receivable recognized by the lessor would include amounts payable under contingent rental arrangements and that the amount of contingent rentals would be reassessed at each reporting date. The Boards had also previously tentatively decided that residual value guarantees would be accounted for in the same manner as contingent rental arrangements. At this meeting, the Boards discussed how to account for

changes in the obligation/receivable arising from reassessment of contingent rentals.

Lessees

The Boards tentatively decided that:

- Adjustments to the obligation to pay rentals as a result of a change in the amount of contingent rentals arising from current or prior periods would be recognized in profit or loss. All other changes would be recognized as an adjustment to the right-of-use asset. This approach is consistent with accounting for changes in estimates. The staff used the following example in the agenda paper to illustrate this approach. If rentals are contingent on sales, an increase in the obligation to pay rentals arising from increased sales in the current and prior periods would be recognized in profit or loss. However, an increase in the estimated obligation to pay rentals arising from increases in forecasted future sales would be recognized as an adjustment to the right-of-use asset.
- Adjustments to the estimated obligation to pay rentals as a result of changes in amounts payable under residual value guarantees would be recognized in the same manner as contingent rental arrangements

Lessors

The Boards tentatively decided that changes in the lessor's receivable arising from changes in contingent rentals would be treated as adjustments to the original transaction price and would be allocated to the lessor's performance obligation. If a change is allocated to a satisfied performance obligation, the effect would be recognized in revenue. However, if a change in the lease receivable is allocated to an unsatisfied performance obligation; the carrying amount of the lessor's performance obligation would be adjusted.

The staff was instructed to provide additional analysis on when a lessor's performance obligation is satisfied in a lease contract.

Determining when contracts are purchases or sales of the underlying asset

At a prior meeting, the Boards had tentatively decided that contracts that represent the purchase or sale of the underlying asset would be excluded from the proposed new lease requirements. The Boards had also previously tentatively decided that transactions that transfer control of the underlying asset would be considered purchases or sales.

At this meeting, the Boards tentatively decided to clarify in the proposed new lease requirements that a contract would be considered a purchase or sale if at the end of the contract, the contract transfers either of the following:

- Control of the underlying asset
- All but a trivial amount of the risks and benefits associated with the underlying asset
- The Boards also tentatively decided that control of the underlying asset would generally be considered transferred/obtained for contracts
- That automatically transfer the title of the underlying asset to the lessee
- That include a bargain purchase option, provided it is reasonably certain that the option will be exercised
- In which the lessor's return would be fixed
- In which it is reasonably certain that the contract will cover the expected useful life of the asset and any risks or benefits associated with the underlying asset that would be retained by the lessor at the end of the contract would not be expected to be more than trivial

The Boards also discussed whether very long leases of land would be considered purchases or sales. The Boards tentatively decided that these leases would not be considered purchases or sales. However, the staff was asked to develop possible criteria for excluding very long leases of land from the scope of the proposed new leases requirements.

Defining initial direct costs

The Boards tentatively decided that *initial direct costs* would be defined as incremental costs directly attributable to negotiating and arranging a lease. The Boards also tentatively decided to include additional guidance to illustrate the types of costs that could be considered initial direct costs.

Defining the interest rate implicit in the lease

The Boards discussed the definition of the *interest rate implicit in the lease* in light of the proposed right-of-use model. The Boards tentatively decided that the rate the lessor would use to discount lease payments would be the rate that the lessor is charging the lessee. That rate would take into account the nature of the transaction and the specific terms of the lease, such as rental payments, lease term, and contingent rentals. The Boards also tentatively decided to include guidance on how to determine the discount rate for different scenarios.

Transitional provisions for lessees

At the June 2009 joint meeting, the Boards tentatively decided that on the date of initial application of the proposed new lease standard a lessee would recognize and measure an obligation to pay rentals and a right-of-use asset for all outstanding leases as follows:

- The obligation to pay rentals would be measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate on the transition date

- The right-of-use asset would be measured on the same basis as the liability, subject to any adjustments required to reflect impairment

At this meeting, the Boards tentatively decided that:

- Assets and liabilities for simple finance/capital leases (those that do not have options, contingent rentals, and/or residual value guarantees) would not be accounted for by applying the new requirements (the recorded assets and liabilities under a finance lease would remain the same on the transition date and the subsequent accounting would not change)
- Assets and liabilities for leases currently accounted for as finance/capital leases, other than simple finance/capital leases, would be subject to the proposed transition requirements
- Finance leases that have been revalued under the revaluation model in IAS 16, *Property, Plant and Equipment*, can use the revaluation amount as the carrying amount of the asset for simple finance/capital leases at transition (the revaluation would not need to be reversed)
- Additional adjustments for prepaid or accrued rentals would be made when lease payments are uneven over the lease term

The Boards will discuss lessee and lessor accounting further at their March 2010 meeting.

See the [IASB project summary](#) for more information on this project.

Revenue recognition

The Boards discussed the scope of the proposed revenue recognition model and the transition requirements for the new revenue recognition standard.

Scope

One of the main objectives of the revenue recognition project is to provide a single revenue recognition model that would apply to a number of industries. To accomplish that objective, the Discussion Paper, *Preliminary Views on Revenue Recognition in Contracts with Customers*, proposed a scope that would apply to revenue arising from contracts with customers. Considering that the proposed definition of a *contract* in the Discussion Paper is “an agreement between two or more parties that creates enforceable obligations,” and the proposed definition of a *customer* is a “party that has contracted with an entity to obtain an asset (such as a good or service) that represents an output of the entity’s ordinary activities,” the proposed scope could be quite broad. Therefore, the Boards discussed what contracts with customers would be in the scope of the proposed new model.

The Boards tentatively decided that the scope of the proposed model would exclude accounting for contracts with customers that are:

- Lease contracts within the scope of IAS 17, *Leases*, or FASB ASC Topic 840, *Leases*
- Insurance contracts within the scope of IFRS 4, *Insurance Contracts*, or FASB ASC Topic 944, *Financial Services-Insurance*
- Contracts within the scope of IFRS 9, *Financial Instruments*, IAS 39, *Financial Instruments: Recognition and Measurement*, or FASB ASC Topic 825, *Financial Instruments*
- Guarantees (other than product warranties) within the scope of IFRS 4, IAS 39, or FASB ASC Topic 460, *Guarantees*

The Boards also discussed accounting for a contract that includes some

performance obligations that would be within the scope of the proposed model and others that would be within the scope of other standards. An example the staff mentioned in the agenda paper for the meeting is a contract that grants a financial instrument to a customer and provides the customer with investment management services. The Boards did not reach a tentative decision on this topic and plan to discuss it further at a future meeting.

Transition

The Boards discussed alternatives for transition and tentatively decided that an entity would apply the proposed standard on a retrospective basis in accordance with IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors* and FASB ASC Topic 250, *Accounting Changes and Error Corrections*. Therefore, in the first financial statement following the effective date, an entity would apply the proposed standard to all contracts in existence at the beginning of the earliest period presented in those financial statements and all contracts entered into after the start of the earliest period presented.

The Boards discussed whether early adoption of the proposed standard would be permitted. The FASB tentatively decided not to permit early adoption of the proposed standard. The IASB did not reach a tentative decision on whether to permit early adoption by entities already applying IFRS. The IASB will discuss this topic at a future meeting.

Because of the requirements of IFRS 1, *First-time Adoption of International Financial Reporting Standards*, the IASB also discussed early adoption by first-time adopters of IFRS. The IASB tentatively decided to permit early adoption of the proposed standard by first-time adopters of IFRS. If this tentative decision is included in a final standard, first-time adopters will be able to avoid the burden of transitioning to the existing IFRS on revenue at first-time adoption and then applying the revised revenue recognition standard at the effective date.

Next steps

At their March 2010 joint meeting, the Boards plan to continue their discussions on disclosure, scope, and contract costs.

See the [IASB project summary](#) for more information on this project.

Right of offset

The IASB and FASB held a joint education session on the netting provisions in Master Agreements, specifically ISDA Master Agreements that govern transactions with central counterparties and to discuss their legal meaning, basis and effect including their commercial effect. Representatives from banks, industry groups and legal experts made presentations to the Boards. The Boards did not make any decisions but the information and understanding gained from this session should help the Boards in any future deliberations that may address the accounting for right of offset.

Future IASB meetings

The IASB held subsequent meetings (some of them jointly with the FASB) on March 3, 11, and 15-24, 2010 and on April 8, 2010. The next IASB meeting is April 19-23, 2010.

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