



On the Horizon for IFRS

October 6, 2008

IFRIC issues September 2008 meeting highlights

IFRIC completes redeliberations of Draft Interpretation on distributions of non-cash assets to owners

IFRIC continues discussions of Draft Interpretation on customer contributions

Customer-related intangible assets discussed

Educational session conducted on regulatory assets and liabilities

Agenda decisions

Tentative agenda decisions

Work in progress

Future Committee meeting

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All decisions reached at IFRIC meetings are tentative and may be changed or modified at future meetings. Committee decisions become final only after completion of a formal vote on an Interpretation or Draft Interpretation, which is confirmed by the IASB.

The International Financial Reporting Interpretations Committee has issued the September 2008 [IFRIC Update](#), which summarizes the Committee's meeting in London on September 4-5, 2008. Highlights of the meeting are discussed below.

IFRIC completes redeliberations of Draft Interpretation on distributions of non-cash assets to owners

The IFRIC completed its redeliberations of Draft Interpretation D23, *Distributions of Non-cash Assets to Owners* (the draft interpretation or D23), and discussed the following proposed revisions:

- The scope of D23 would be clarified with respect to common control transactions

- Measurement of the dividend payable would be specified without attributing the requirement to a particular standard and also modifying the disclosure requirements
- An additional rationale would be provided for the conclusion that the settlement gain should be included in profit or loss
- Guidance would be added on when to recognize the dividend payable
- Proposed amendments to IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, would add guidance for assets classified as held for distribution to owners

The IFRIC acknowledged respondents' comments about the potential accounting mismatch in equity that would result from measuring the assets to be distributed at their carrying amount and measuring the dividend payable at the fair value of the assets to be distributed. The IFRIC decided not to recommend that the IASB amend IFRS 5 to require that the assets to be distributed be measured at fair value for the following reasons:

- No IFRS literature supports an upward remeasurement of assets solely on the basis of a commitment to distribute and upward remeasurement would be inconsistent with the accounting in IFRS 5 for assets held for distribution.
- Any accounting mismatch created when the dividend payable is recognized would exist only during the normally short period until the liability is settled.

The IFRIC concluded that the proposed revisions did not require re-exposure of the draft interpretation. The IFRIC voted to confirm the consensus and asked the staff to present the final draft interpretation to the IASB for ratification. The staff expects that the final Interpretation will apply prospectively for distributions recognized in annual periods that begin on a date

three months or more after it is issued. Retrospective application will not be permitted. Early application will be allowed.

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

IFRIC continues discussions of Draft Interpretation on customer contributions

The IFRIC continued its discussions of the staff's analysis and rationale for a revised Draft Interpretation D24, *Customer Contributions* (the draft interpretation or D24), and also considered two illustrative examples.

Issues discussed at the July 2008 meeting

At the July 2008 meeting, the IFRIC discussed comments received on D24 and an example of a customer contribution for connection to a price-regulated network. The IFRIC reached the tentative view on this specific example that the ongoing obligation to provide access arises from the terms of the operating license, not from the contribution. The accounting for the resulting credit when an asset is recognized was also discussed at the July 2008 meeting. When the contributed asset is recognized because the entity controls that asset, then the entity must consider how to account for the resulting credit. If a performance obligation does not remain after the connection has been established, then the resulting credit would be to revenue when the connection is made. For discussion at the September 2008 meeting, the IFRIC directed the staff as follows:

- Develop indicators based on IAS 18 to determine whether connection services would be better identified as a separate component from the ongoing service of providing access to the network
- Prepare additional examples

- Carryover the proposals in D24 with respect to recognition and measurement of the contributed asset

Issues discussed at the September 2008 meeting

At the September 2008 meeting, the staff presented a revised draft interpretation that included the following issues, which resulted from the July 2008 meeting:

Clarifying the scope of D24 and simplifying the analysis for recognition and measurement of a contributed asset

The respondents to D24 generally did not object to the proposals; however they believed that D24 was complex and difficult to understand and apply. The staff discussed the various proposed steps in D24 that determine whether an asset should be recognized, including the consideration of IFRIC 4, *Determining whether an Arrangement contains a Lease* and IAS 17, *Leases*. The staff proposed that the IFRIC should simplify D24 and address the issue of who controls the asset by proposing guidance based on the *Framework* and existing IFRS. The IFRIC generally agreed with the staff's proposal that an approach that deals with who controls the asset is easier to understand than the step-by-step approach that is presently included in D24. However, the IFRIC asked the staff to

- Identify whether other indicators should be added to the revised draft
- Ensure that the guidance developed in D24 is consistent with guidance on similar issues in IFRS, specifically in guidance for arrangements where the asset is controlled only for a portion of its useful life

Identifying the different components of a single transaction in accordance with IAS 18

The staff proposed an approach to identify the different components of a single transaction in accordance with IAS 18, *Revenue*. The IFRIC supported this proposed approach and took the view that indicators would be useful. Those

indicators would help to identify the goods or services to be provided in exchange for the customer contribution:

- *Some features indicate that there may be only one service delivered:* For example, connection to the network in a rate-regulated environment or ongoing services provided at a reduced rate in an outsourcing arrangement
- *Other features indicate that there may be two services delivered:* For example, the initial connection to the network and the service to provide ongoing access to a supply of goods or services

The IFRIC asked the staff to refine the wording of the proposed indicators, add references in the illustrative examples to the revised draft interpretation, and develop an example of a customer contribution arising in an outsourcing arrangement.

Determining the period over which revenue should be recognized if an ongoing service is part of the arrangement

The staff presented the issue of determining the period over which revenue should be recognized when an ongoing service is part of the arrangement. The IFRIC concluded that the period for revenue recognition should generally be determined by the terms of the arrangement with the customer. However if the arrangement does not specify a period, then revenue should be recognized over a period not longer than the useful economic life of the contributed asset used to provide the ongoing service.

At the November 2008 meeting, the staff plans to present a revised draft interpretation that will include the IFRIC's tentative views, a basis for conclusions, and illustrative examples.

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

Customer-related intangible assets discussed

The IFRIC received a request for guidance regarding the circumstances in which a non-contractual customer relationship arises in a business combination. In accordance with IFRS 3, *Business Combinations* (as revised in 2008), an acquirer recognizes the identifiable intangible assets of the acquiree separately from goodwill. An intangible asset is identifiable if it meets either the contractual-legal criterion or the separable criterion in IAS 38, *Intangible Assets*.

Determining whether a customer relationship is contractual or noncontractual can be critical when distinguishing between intangible assets and goodwill, because noncontractual customer relationships are recognized separately from goodwill only if they meet the separable criterion (i.e. the customer relationships are capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability).

The IFRIC staff has determined that there is diversity in practice with respect to determining which customer relationships have a contractual basis. In part, this may be a consequence of valuation experts having different views. Therefore, the IFRIC agreed with the staff that this issue should be added to the agenda and that the outcome of this project would not necessarily be an Interpretation. The IFRIC staff will work with the FASB staff and consider the deliberations of appraisal/valuation professional organizations to develop a project proposal for presentation at the IFRIC meeting in November 2008.

Educational session conducted on regulatory assets and liabilities

At the May 2008 meeting, the IFRIC approved a project plan to consider whether regulated entities could or should recognize a liability (or an asset) as a result of price regulation by regulatory bodies or governments. The September 2008 meeting included an educational session on this topic and no decisions

were reached by the IFRIC. The IFRIC considered the background information accumulated as a result of the staff's research. In order to assess whether this issue should be added to the agenda, the IFRIC identified several matters that they believe the staff should further analyze. At the November 2008 meeting, the staff will present a paper discussing their recommendation on whether this issue should be added to the IFRIC agenda.

Agenda decisions

IFRIC agenda decisions are not Interpretations, which are determined only after deliberation and due process, including a formal vote. IFRIC Interpretations become final only when approved by the IASB.

At the July 2008 meeting, the IFRIC had tentatively decided not to add three issues to the agenda at that time and to reconsider them at the September 2008 meeting. The Committee discussed the issues at the September 2008 meeting.

IAS 17, Leases – Time pattern of the user's benefit

The Committee received a request for guidance on alternatives to straight-line recognition of lease expense. IAS 17.34 states that

For operating leases, lease payments (excluding costs for services such as insurance and maintenance) are recognised as an expense on a straight-line basis unless another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis.

The Committee indicated that guidance had previously been requested on this issue and had not been added to the agenda for the following reasons:

- IAS 16, *Property, Plant and Equipment*, and IAS 38, *Intangible Assets*, require an entity to recognize the use of productive assets using the method that best reflects “the pattern in which the asset’s future economic benefits are expected to be consumed by the entity”
- IAS 17, in contrast, refers to the time pattern of the user’s benefit

Based upon the existing IFRS guidance, any alternative to the straight-line method of recognizing operating lease expense must reflect the time pattern of the use of the leased property rather than the amount of use or other factor related to economic benefits.

The Committee decided not to add this issue to the agenda since it did not expect significant diversity in practice.

IAS 18, Revenue and IAS 39, Financial Instruments: Recognition and Measurement – Accounting for trailing commissions

The Committee received a request to provide guidance on the accounting by an entity for ongoing commission arrangements (trailing commissions). The issue specifically relates to the accounting treatment where the contractual obligation for the payment/receipt of the commission is not linked to the performance of any future service (for example, when a financial adviser directs its client’s funds to an investment manager’s product). In this type of arrangement, the financial adviser would receive both an initial commission for the placement of the business with the investment manager and an ongoing (trailing) commission, provided that the client’s funds remain invested in the product for a specified time.

The IFRIC noted that many industries have similar arrangements and that practice is diverse, since it is difficult to determine whether the entity is required to provide any future service to be entitled to receive the commission. Diversity

also arises because IAS 18 and IAS 39 have different recognition criteria and views differ on whether IAS 18 or IAS 39 is the relevant standard.

The IFRIC decided not to add this issue to the agenda for the following reasons:

- The IFRIC would not be able to reach a consensus on a timely basis due to the complexity and pervasiveness of the issues.
- The IASB is considering the issues in its revenue recognition and liabilities projects.

IAS 32, Financial Instruments: Presentation – Transaction costs to be deducted from equity

The Committee received a request to provide guidance on

- The extent of transaction costs to be accounted for as a deduction from equity in accordance with IAS 32.37, as follows:
The transaction costs of an equity transaction are accounted for as a deduction from equity (net of any related income tax benefit) to the extent they are incremental costs directly attributable to the equity transaction that otherwise would have been avoided.
- The allocation of transaction costs that relate jointly to more than one transaction in accordance with IAS 32.38, as follows:
Transaction costs that relate jointly to more than one transaction (for example, costs of a concurrent offering of some shares and a stock exchange listing of other shares) are allocated to those transactions using a basis of allocation that is rational and consistent with similar transactions.

The issues relate specifically to the meaning of the terms *incremental* and *directly attributable*. The Committee indicated that IAS 32 provides the following:

- Only incremental costs directly attributable to issuing new equity instruments or acquiring previously outstanding equity instruments are related to an equity transaction.
- Judgement will be required to determine which costs are related solely to other activities undertaken at the same time as issuing equity (e.g., becoming a public company or acquiring an exchange listing) and which are costs that relate jointly to more than one transaction that must be allocated.

Based upon the existing IFRS guidance, the Committee decided not to add this issue to the agenda. The IFRIC noted that the terms *incremental* and *directly attributable* are used with similar but not identical meanings in many of the IFRS and therefore recommended that the IASB develop common definitions for both terms and add them to the Glossary as part of the annual improvements project.

Tentative agenda decisions

After reviewing the following issues, the Committee tentatively decided not to add them to the agenda at this time. The issues will be reconsidered at the November 2008 meeting.

IAS 39, Financial Instruments: Recognition and Measurement – Valuation of restricted securities

The Committee received a request for guidance on whether a discount must be applied to the quoted market price when establishing the fair value of a security quoted in an active market when there is a contractual, governmental, or other legally enforceable restriction that prevents the sale of the security for a specified period. The request asked for guidance with respect to situations in

which the restriction applied to the current holder of the security and would not transfer to another entity.

The Committee decided not to add this issue to the agenda because in this case any guidance it could provide would be implementation guidance; not interpretative guidance. The IASB should provide any necessary guidance in its fair value measurement project.

IFRIC 14, IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction – Stable workforce assumption

The Committee received a request for guidance regarding the economic benefit available in the form of reductions in future contributions when there is a minimum funding requirement. IAS 19, *Employee Benefits* limits the asset that an entity can recognize for a surplus in a defined benefit pension plan to the present value of the economic benefit available from both refunds from the plan and reductions in future contributions to the plan. In determining the future service cost, IFRIC 14 requires that the economic benefit available should be determined assuming a stable workforce unless the entity is demonstrably committed at the end of the reporting period to reduce the number of covered plan employees.

The request indicates that there could be circumstances where the stable workforce assumption understates the economic benefits available, affecting both the statement of financial position and profit or loss. Plan contributions that are regarded under IFRIC 14 as providing no economic benefits are recognized as an expense, not an asset. Therefore, an entity could affect its reported earnings by choosing the timing and the level of such contributions.

The Committee decided not to add this issue to the agenda for the following reasons:

- The IFRIC 14 requirements with respect to the assumption of a stable workforce are clear and had been discussed at length during the development of the interpretation. In addition, the request for guidance did not provide any new information to be considered.
- The effect of the timing of voluntary contributions (as described in the request) is an inherent part of the limit on the asset that can be recognized with respect to the surplus in accordance with IAS 19.

Work in progress

The Committee reviewed a summary of the remaining outstanding issues, as follows:

- *European Regulation concerning Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH)*: The Committee along with other

interpretive bodies will shortly begin discussing the REACH compliance costs issue.

- *Group cash-settled share-based payment transactions*: The IASB will consider the Committee's recommendations on group cash-settled share-based payment transactions at its September 2008 meeting.
- *Application of the effective interest rate method*: In October 2008, the staff expects to make recommendations to the IASB on the application of the effective interest rate method.
- *Derecognition*: The Committee agreed with the staff's proposal that it should consider removing derecognition from its agenda given the acceleration of the IASB's project. The staff will make a recommendation concerning this issue at the November 2008 Committee meeting.

Future Committee meeting

The next Committee meeting is November 6-7, 2008.