IFRIC Update

From the IFRS Interpretations Committee

January 2011

Welcome to the IFRIC Update

IFRIC Update is published as a convenience to the IASB's constituents. All conclusions reported are tentative and may be changed or modified at future IFRS Interpretations Committee meetings.

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

The IFRS Interpretations Committee met in London on **6 and 7 January**, when it discussed:

- Current agenda:
  - Accounting for stripping costs in the production phase of a surface mine
  - Contingent pricing of property, plant and equipment and intangible assets
  - Put options written over non-controlling interests
- IFRS Interpretations Committee tentative agenda decisions
- Issues considered for *Annual Improvements*
- IFRS Interpretations Committee work in progress

Contact us

IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH
United Kingdom

Tel: +44 (0)20 7246 6410
Fax: +44 (0)20 7246 6411
E-mail: **ifric@ifrs.org**
Website: **www.ifrs.org**

Future IFRS Interpretations Committee meetings

The next meetings are:
10 and 11 March 2011
5 and 6 May 2011
7 and 8 July 2011
8 and 9 September 2011
3 and 4 November 2011

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Current agenda:

The Interpretations Committee discussed the following issues which are on its current agenda.

IAS 16 *Property, Plant and Equipment* - Accounting for stripping costs in the production phase of a surface mine

The Committee took this issue onto its agenda in November 2009, and in August 2010 it published for public comment a Draft Interpretation *Stripping Costs in the Production Phase of a Surface Mine*. The 90 day comment period ended on 30 November 2010. At the January 2011 meeting, the staff presented a comment letter summary to the Committee of the comments received on the Draft Interpretation.

The Committee discussed the issues raised by the respondents, and it agreed to continue deliberating comments received on the Draft Interpretation. To this end, the Committee asked the staff to bring the following matters back for further discussion at the March 2011 Committee meeting:

- A description of the principle for the capitalisation of production stripping costs that did not require definition of nor reference to the term 'stripping campaign', including guidance on the apportionment of costs incurred between ore that is mined in the period (inventory) and the improved access to ore to be mined in the future (long-term asset), and
- A refined approach for depreciation/amortisation of the capitalised costs, along the lines of the specific identification approach described in the Draft Interpretation.

IAS 16 *Property, Plant and Equipment and IAS 38 Intangible Assets* - Contingent pricing of property, plant and equipment and intangible assets

The Committee received a request asking for guidance on how to account for contingent pricing for the outright purchase of a single item of property, plant and equipment (PPE) or intangible asset. The issues include (i) when to record the liability for such contingent prices and (ii) whether subsequent changes to the contingent price, when recognised, should be recognised in profit or loss or as an adjustment to the cost of the asset purchased.

The Committee noted a lack of specific guidance in current IFRSs in relation to contingent prices, for transactions that are not business combinations. It discussed the application of the general requirements in IFRSs with respect to the cost model for PPE and intangible assets and the recognition and measurement of financial liabilities.

As part of its discussions, the Committee noted that while certain contingent price arrangements would meet the definition of a financial liability, others would not. It also noted that the timing at which the criteria for recognition of an asset are met might differ from that for a financial liability. With respect to subsequent changes, it noted that IAS 39 *Financial Instruments: Recognition and Measurement* requires changes to a financial liability recognised for the contingent price payable to be recorded in profit or loss. Some viewed this as being in conflict with the cost model in IAS 16, as they hold the view that IAS 16 requires that the actual amount paid be considered part of the cost recognised for the asset.

Having assessed the issue against the Interpretations Committee's agenda criteria, the Committee decided to take the issue onto its agenda with a view to developing an interpretation on the accounting for contingent prices arising from the purchase of single assets.

The Committee discussed several possible paths forward, including:

- an analogy to IFRS 3 *Business Combinations* which would require the cost of the asset to include the fair value of the contingent consideration at the date of purchase, with subsequent changes to the contingent consideration being recognised in profit or loss.
- an analogy to IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* which would require the cost of the asset to include an estimate of the contingent consideration at the date of purchase, with subsequent changes to the liability, to the extent that they do not reflect the passage of time, be adjusted against the cost of the asset.

At the next meeting in March 2011, the Committee will discuss:

- the scope of the project, and
- alternatives for the accounting for contingent prices for the purchase of a single item of PPE.

IAS 32 *Financial Instruments: Presentation* - Put options written over non-controlling interests

Over recent meetings the Committee has discussed aspects of the accounting for put options written over non-controlling interests (NCI puts) in the consolidated financial statements of the controlling shareholder. Constituents have expressed concern about the diversity in accounting for the subsequent measurement of the financial liability recognised for NCI puts.

At the November 2010 IASB meeting, the Board expressed support for the Committee to work with the staff of the Financial Instruments with Characteristics of Equity (FICE) project team to develop a short-term solution to the issue. At the January 2011 Committee meeting, the Committee received an education session from the staff of the FICE team to learn of their views on the possible direction and timing of the FICE project so that it could consider how this might influence its decisions on the next steps for its work on NCI puts.

The Committee discussed possible paths forward including consideration of a scope exception from IAS 32. The Committee asked the staff to bring the following matters back for further discussion at the March 2011 Committee meeting:

- consider the viability of a scope exception from IAS 32; and
- should a scope exception be viable, whether an interpretation would then be needed to specify the

accounting for NCI puts.

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IFRS Interpretations Committee tentative agenda decisions

The Committee reviewed the following matters and tentatively decided that they should not be added to the Committee's agenda. These tentative decisions, including recommended reasons for not adding the items to the Committee's agenda, will be reconsidered at the Committee meeting in March 2011. Constituents who disagree with the proposed reasons, or who believe that the explanations may contribute to divergent practices, are encouraged to communicate those concerns by ***14 February 2011*** *by email to:* ***ifric@ifrs.org****. Communications will be placed on the public record unless the writer requests confidentiality, supported by good reason, such as commercial confidence.*

IAS 8 *Accounting Policies, Changes in Accounting estimates and Errors* – Application of the IAS 8 hierarchy

IAS 8 requires that management use judgement in developing and applying an accounting policy that is relevant and reliable, in the absence of an IFRS that specifically applies to a transaction. IAS 8 specifies that management shall refer to and consider the applicability of requirements in IFRSs dealing with similar and related issues. The Committee received a question as to whether it could be appropriate to only consider certain aspects of an IFRS being analogised to, or whether all aspects of the IFRS being analogised to would be required to be applied.

The Committee observed that when management develops an accounting policy through analogy to an IFRS dealing with similar and related matters, it needs to use its judgement and apply all aspects of the IFRS that are relevant to the particular issue.

The Committee concluded that the process for developing accounting policies by analogy does not need to be clarified in paragraphs 10–12 of IAS 8 because the current guidance is sufficient.

Therefore, the Committee [decided] that this issue should not be added to its agenda.

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* – Inclusion of own credit risk in the discount rate

The Committee received a request for interpretation of the phrase 'the risks specific to the liability' and whether this means that an entity's own credit risk (performance risk) should be excluded from any adjustments made to the discount rate used to measure liabilities. The request assumed that future cash flow estimates have not been adjusted for the entity's own credit risk.

The Committee observed that paragraph 47 of IAS 37 states that 'risks specific to the liability' should be taken into account in measuring the liability. The Committee noted that IAS 37 does not explicitly state whether or not own credit risk should be included. The Committee also noted that the predominant practice today is to exclude own credit risk which is generally viewed in practice as a risk of the entity rather than a risk specific to the liability. Accordingly, the Committee does not expect significant diversity in practice, and therefore [decided] not to add this issue to its agenda.

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Issues considered for *Annual Improvements*

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

In August 2010, the Trustees of the IFRS Foundation published for public comment a Consultation Document which sets out a proposal to add new paragraphs to the Due Process Handbook for the International Accounting Standards Board *(IASB Due Process Handbook) relating to the annual improvements process. The proposed amendments to the IASB Due Process Handbook are intended to provide enhanced criteria to assist the IASB and interested parties in determining whether a matter relating to the clarification or correction of IFRSs should be addressed using the annual improvements process. The Consultation Document sought views on the sufficiency and appropriateness of these proposed criteria.*

Annual Improvements Criteria – Comment letter summary

The staff presented the Committee with a summary of the comments received on the proposed amendments to the IASB Due Process Handbook, asking for its views, to help shape recommendations to the Trustees. The Committee suggested modifications to the following aspects of the proposed qualifying criteria for annual improvements:

a. to remove wording that states that a correcting amendment may create an exception from an existing principle;
b. to refine wording to emphasise that the scope of an amendment should be sufficiently narrow;
c. to remove the word ‘pressing’ when considering the need to make an amendment sooner than an IASB project would.

The Committee also discussed other supplemental criteria that could be used to clarify the distinction between an annual improvement and an interpretation.

The Committee members’ views will be discussed with the Board at its January 2011 meeting. The Board members’ views, together with those of the Committee members will, in turn, be included in the recommendations to the IFRS Foundation’s Trustees.

Issue with recommendation to be added to *Annual Improvements*

IAS 1 *Presentation of Financial Statements* – Current/non-current classification of debt (roll-over agreements)

In October 2010, the Committee received a request for guidance on the meaning of ‘unconditional right to defer settlement’ in paragraph 69(d) of IAS 1. The issue was discussed at the Committee meeting in November 2010. In its deliberations, the Committee also considered a practical application of the issue, involving the classification of a short-term obligation (commercial paper) when it is backed by a long-term loan facility. At that meeting, the Committee requested that the staff perform outreach on the topic in order to understand the level of diversity in practice, and to bring the issue back for further consideration at its meeting in January 2011.

At the January 2011 meeting, the staff presented to the Committee the results of the outreach performed with some members of the National Standard Setters’ group. The Committee noted that there is no diversity arising from the application of paragraph 73 of IAS 1, except in circumstances where an existing loan facility is renegotiated with the same lender, but at different terms. The Committee decided to recommend that the Board amend the wording of paragraph 73 through *Annual Improvements*. This amendment would clarify that where an entity renegotiates an existing loan for at least 12 months after the reporting period, with the same lender at the same or similar terms, it classifies the loan as non-current.

Issue with recommendation not to be added to *Annual Improvements*

The Committee deliberated an additional issue for consideration within Annual Improvements*. The Committee decided to recommend that the Board should not add the following issue to* Annual Improvements:

IFRS 3 *Business Combinations and IAS 39 Financial Instruments: Recognition and Measurement* - Hedging the foreign exchange risk in a business combination

The IFRS Interpretations Committee received a request to clarify the application of IAS 39 hedge accounting to the gains or losses arising from hedging the foreign exchange risk in relation to the amount of the consideration paid in a business combination. The question considered is whether the gains or losses from the hedging instrument would result in an adjustment to the amount that is recognised for goodwill.

The Committee noted that paragraph AG98 of IAS 39 allows an entity to apply hedge accounting when hedging the movements in foreign currency exchange rates for a firm commitment to acquire a business in a business combination. The Committee also noted that when a basis adjustment is made to a hedged item in accordance with IAS 39 hedge accounting, it is after other applicable IFRSs have been applied. Accordingly, such a basis adjustment is made to goodwill (or the gain from a bargain purchase) after the application of the guidance in IFRS 3.

The Committee considered that IAS 39 provides sufficient guidance on the accounting for hedging transactions that it does not expect diversity in practice. Therefore, the Committee proposed that the issue should not be included in *Annual Improvements*.

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IFRS Interpretations Committee work in progress

Committee outstanding issues update

The Committee received a report of outstanding issues. These issues included a follow up of the issue discussed at the November 2010 Committee meeting relating to IFRS 2 *Share-based Payments* – share-based payment awards settled net of tax withholding. The other issue is a new item raising concerns about diversity in practice in the application of the notion of continuous transfer in the context of IFRIC 15 *Agreements for the Construction of Real Estate*. The staff expects to bring both of these matters to the March 2011 Committee meeting for discussion.

With the exception of these two issues, all requests received and considered by the staff were discussed at this meeting.

Future IFRS Interpretations Committee meetings: 2011

The Committee's meetings are expected to take place in London, UK as follows:

- **10 and 11 March 2011**
- **5 and 6 May 2011**
- **7 and 8 July 2011**
- **8 and 9 September 2011**
- **3 and 4 November 2011**

Meeting dates, tentative agendas and additional details about the next meeting will also be posted to the IASB website at www.ifrs.org before the meeting. Instructions for submitting requests for Interpretations are given on the IASB website at:
http://www.ifrs.org/How+we+develop+Interpretations/Propose+an+agenda+item.htm.

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