STAFF PAPER

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IASB Meeting

Project	**Annual Improvements project –2011-2013 cycle**
Paper topic	Proposed wording for final amendments–changes tracked to Bound Volume

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Introduction

1. This paper sets out the proposed wording for annual improvements project issues discussed and confirmed by the IFRS Interpretations Committee (the Interpretations Committee) for inclusion in the final *Improvements to IFRSs* that is planned to be issued in Q4 2013.

2. In this paper, changes are marked-up based on the text included in the (red) Bound Volume as of 1 January 2013. New text is underlined and deleted text is ~~struck through~~.

Amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards*

The IASB proposes to amend the Basis for Conclusions on IFRS 1 *First-time Adoption of International Financial Reporting Standards*, which is not part of the Standard, by adding a footnote to paragraph BC11 and adding paragraph BC11A. New text is underlined and deleted text is struck through.

BC11 Paragraphs 7–9 of the IFRS require a first-time adopter to apply the current version of IFRSs, without considering superseded or amended versions[1]. This:

(a) enhances comparability, because the information in a first-time adopter's first IFRS financial statements is prepared on a consistent basis over time;

(b) gives users comparative information that was prepared using later versions of IFRSs that the IASB regards as superior to superseded versions; and

(c) avoids unnecessary costs.

BC11A Paragraph 7 requires an entity to use the IFRSs that are effective at the end of its first IFRS reporting period. Paragraph 8 allows a first-time adopter to apply a new IFRS that is not yet mandatory if that IFRS permits early application. Notwithstanding the advantages set out in paragraph BC11 of applying a more recent version of an IFRS, paragraphs 7 and 8 permit an entity to use either the currently mandatory IFRS or the new IFRS that is not yet mandatory, if that IFRS permits early application. Paragraph 7 requires an entity to apply the same version of the IFRS throughout the periods covered by the entity's first IFRS financial statements. Consequently, if a first-time adopter chooses to early apply a new IFRS, that new IFRS will be applied throughout the periods presented in its first IFRS financial statements, unless IFRS 1 provides an exemption or an exception that permits or requires otherwise.

[1] This paragraph does not require an entity to use a more recent version of an IFRS. It only explains the advantages of applying a more recent version of an IFRS. See paragraph BC11A for further details.

Amendment to IFRS 3 *Business Combination*

Paragraph 2 is amended and paragraph 64H is added. New text is underlined and deleted text is struck through.

Scope

2 This IFRS applies to a transaction or other event that meets the definition of a business combination. This IFRS does not apply to:

(a) <u>the accounting for</u> the formation of a <u>joint arrangement</u> ~~joint venture~~ <u>in the financial statements of the joint arrangement itself</u>.

(b) ...

Effective date

…

<u>64H</u> <u>*Annual Improvements Cycle 2011–2013* issued in [date] amended paragraph 2(a). An entity shall apply that amendment prospectively for annual periods beginning on or after 1 July 2014. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.</u>

Basis for Conclusions on the amendment to IFRS 3 *Business Combinations* (as revised in 2008)

This Basis for Conclusions accompanies, but is not part of, the proposed amendment.

Scope

BC61A The IASB observed that there was uncertainty about whether paragraph 2(a) of IFRS 3, which excludes the formation of joint ventures from the scope of IFRS 3, should have been amended to refer to joint arrangements when IFRS 11 was issued. The IASB did not change the wording of the scope exclusion in paragraph 2(a) of IFRS 3 for 'the formation of a joint venture' when it replaced IAS 31 *Interests in Joint Ventures* with IFRS 11 *Joint Arrangements*, although it intended not to change the scope of IFRS 3. IFRS 11 had changed the use of the term 'joint venture' from having a general meaning that included 'jointly controlled operations', 'jointly controlled assets' and 'jointly controlled entities', to meaning a specific type of joint arrangement, which does not include 'joint operations'.

BC61B There was also uncertainty about whether the scope exclusion in paragraph 2(a) of IFRS 3 addresses:

(i) the accounting by the joint arrangements themselves in their financial statements only; or

(ii) also the accounting by the parties to the joint arrangement for their interests in the joint arrangement.

BC61C The IASB noted that paragraph 2(a) of IFRS 3 should exclude formations of every type of joint arrangement (ie joint ventures and joint operations) from the scope of IFRS 3. It also noted that paragraph 2(a) of IFRS 3 only excludes from the scope of IFRS 3 the accounting by the joint arrangements themselves in their financial statements. It does not provide a scope exclusion from IFRS 3 for the parties to the joint arrangement; IFRS 3 applies when an entity obtain control over a business, so the scope exclusion is not applicable in the financial statements of the parties to a joint arrangement when the joint arrangement is established because the parties do not obtain control of the joint arrangement..

BC61D The IASB concluded that paragraph 2(a) of IFRS 3 should be amended to address all types of joint arrangements and to remove uncertainty about the financial statements to which it applies.

BC61E Consequently, the IASB amended paragraph 2(a) of IFRS 3 to:

(a) exclude the formation of all types of joint arrangements from the scope of IFRS 3 by replacing 'joint venture' with 'joint arrangement'; and

(b) clarify that it only excludes the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself from the scope of IFRS 3.

Effective date and transition

BC432A The IASB amended paragraph 2 and added paragraph 64H to clarify the scope exception in paragraph 2(a) of IFRS 3. It considered the transitional provisions and effective date of the amendment to IFRS 3. In order to be consistent with the prospective initial application of IFRS 3, the IASB decided that an entity would apply the amendments to IFRS 3 prospectively for annual periods beginning on or after 1 July 2014.

Amendment to IFRS 13 *Fair Value Measurement*

Paragraph 52 is amended and paragraph C4 is added. New text is underlined and deleted text is struck through.

Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk

52 The exception in paragraph 48 applies only to financial assets, ~~and~~ financial liabilities and other contracts within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 9 *Financial Instruments*. The references to financial assets and financial liabilities in paragraphs 48–51 and 53–56 should be read as applying to all contracts within the scope of, and accounted for in accordance with, IAS 39 or IFRS 9, regardless of whether they meet the definitions of financial assets or financial liabilities in IAS 32 *Financial Instruments: Presentation*.

Effective date and transition

C4 *Annual Improvements 2011–2013* cycle, issued in [date], amended paragraph 52. An entity shall apply that amendment prospectively from the beginning of the earliest period presented for which IFRS 13 is applied. An entity shall apply that amendment for annual periods beginning on or after 1 July 2014. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.

Basis for Conclusions on the amendment to IFRS 13 *Fair Value Measurement*

This Basis for Conclusions accompanies, but is not part of, the proposed amendment.

After paragraph BC119 a subheading and paragraphs BC119A–BC119B are added.

Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk

Scope of paragraph 52

BC119A After issuing IFRS 13 the IASB was made aware that it was not clear whether the scope of the exception for measuring the fair value of a group of financial assets and financial liabilities on a net basis (the 'portfolio exception') includes all contracts that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 9 *Financial Instruments*. The exception is set out in paragraph 48 and the scope of the exception is set out in paragraph 52. In particular, questions were raised about whether the scope included contracts that are accounted for as if they were financial instruments, but that do not meet the definitions of financial assets or financial liabilities in IAS 32 *Financial Instruments: Presentation*, such as some contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments.

BC119B The IASB did not intend to exclude such contracts from the scope of the portfolio exception if they are within the scope of IAS 39 or IFRS 9. Consequently, the IASB amended paragraph 52 of this Standard to clarify that the portfolio exception applies to all contracts within the scope of IAS 39 or IFRS 9, regardless of whether they meet the definitions of financial assets or financial liabilities as defined in IAS 32.

Effective date and transition

BC230A The IASB amended paragraph 52 and added paragraph C4 to clarify the scope of the portfolio exception. It considered the transitional provisions and effective date of the amendments to IFRS 13. In order to be consistent with the prospective initial application of IFRS 13, the IASB decided that an entity would apply the amendments to IFRS 13 prospectively from the beginning of the earliest period presented for which IFRS 13 is applied and that an entity should apply that amendment for annual periods beginning on or after 1 July 2014.

Amendment to IAS 40 *Investment Property*

Before paragraph 6, a heading is added. Paragraph 14A is added. After paragraph 84 a heading and paragraph 84A are added. Paragraph 85D is added. Paragraphs 6 and 14 have been included for ease of reference but are not proposed for amendment.

Classification of property as investment property or owner-occupied property

6 **A *property interest* that is held by a lessee under an operating lease may be classified and accounted for as investment property if, and only if, the property would otherwise meet the definition of an investment property and the lessee uses the fair value model set out in paragraphs 33–55 for the asset recognised. This classification alternative is available on a property-by-property basis. However, once this classification alternative is selected for one such property interest held under an operating lease, all property classified as investment property shall be accounted for using the fair value model. When this classification alternative is selected, any interest so classified is included in the disclosures required by paragraphs 74–78.**

…

14 Judgement is needed to determine whether a property qualifies as investment property. An entity develops criteria so that it can exercise that judgement consistently in accordance with the definition of investment property and with the related guidance in paragraphs 7–13. Paragraph 75(c) requires an entity to disclose these criteria when classification is difficult.

14A Judgement is also needed to determine whether the acquisition of investment property is the acquisition of an asset or a group of assets or a business combination within the scope of IFRS 3 *Business Combinations*. Reference should be made to IFRS 3 to determine whether it is a business combination. The discussion in paragraphs 7–14 of this Standard relates to whether or not property is owner-occupied property or investment property and not to determine whether or not the acquisition of property is a business combination as defined in IFRS 3. Determining whether a specific transaction meets the definition of both a business combination as defined in IFRS 3 and includes an investment property as defined in this Standard requires the separate application of both Standards.

...

Transitional provisions

Business Combinations

84A ***Annual Improvements Cycle 2011–2013* issued in [date] added paragraph 14A and a heading before paragraph 6. An entity shall apply that amendment prospectively for acquisitions of investment property from the beginning of the first period for which it adopts that amendment. Consequently, amounts recognised for acquisitions of investment property in prior periods shall not be adjusted. However, retrospective application of that amendment is permitted if and only if information needed to apply the amendment retrospectively is available to the entity.**

Effective date

…

85D *Annual Improvements Cycle 2011–2013* issued in [date] added paragraphs 14A and 84A and a heading before paragraph 6. An entity shall apply those amendments for annual periods beginning on or after 1 July 2014. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

Basis for Conclusions on the proposed amendment to IAS 40 *Investment Property*

This Basis for Conclusions accompanies, but is not part of, the proposed amendment.

Classification of property as investment property or owner-occupied property

Acquisition of investment property: interrelationship with IFRS 3

BC39A The IFRS Interpretations Committee (the Interpretations Committee) reported to the IASB that practice differed in delineating the scope of IFRS 3 *Business Combinations* and IAS 40 *Investment Property*:

(a) Some considered both Standards as mutually exclusive if investment property with associated insignificant ancillary services, as specified in paragraph 11 of IAS 40, is acquired. They view property, together with any associated insignificant ancillary services, as being a single ‘unit of account’ and they consider this unit of account to be one asset called ‘investment property’.

(b) Others did not view IFRS 3 and IAS 40 as being mutually exclusive if investment property with associated insignificant ancillary services, as specified in paragraph 11 of IAS 40, is acquired; nor did they view the definitions of a business as defined in Appendix A of IFRS 3 and investment property as defined in paragraph 5 of IAS 40 as being interrelated. They think that an entity acquiring investment property has to determine whether it meets both definitions.

BC39B The IASB noted that paragraphs 8–14 of IAS 40 have been developed to differentiate investment property from owner-occupied property, or to delineate the scope of IAS 40 to distinguish it from the scope of IAS 16 *Property, Plant and Equipment*. In addition, neither IFRS 3 nor IAS 40 contains a limitation in its scope that restricts its application when the other Standard applies, ie there is nothing within the scope of each Standard to suggest that they are mutually exclusive. The IASB also noted that the wording of IAS 40 is not sufficiently clear about the interrelationship of the two Standards.

BC39C The IASB agrees with the proponents of the view presented in paragraph BC39A(b) that IFRS 3 and IAS 40 are not mutually exclusive. It amended IAS 40 to state explicitly that judgement is also needed to determine whether the transaction is solely the acquisition of an investment property or whether it is the acquisition of a group of assets or a business combination in the scope of IFRS 3 that includes an investment property. That judgement is not based on paragraphs 7–14 of IAS 40 but is instead based on the guidance in IFRS 3. Only the judgement needed to distinguish investment property from owner-occupied property is based on these paragraphs.

BC39D Consequently, the IASB clarified the interrelationship of the two Standards by adding paragraph 14A and a heading before paragraph 6 to IAS 40.

Effective date and transition

BC68 The IASB added paragraphs 14A, 84A and 85D and a heading before paragraph 6 of IAS 40 to clarify the interrelationship between IFRS 3 and IAS 40. It considered the transitional provisions and effective date of the amendment to IAS 40. The IASB noted that applying IFRS 3 to transactions that have previously been accounted for as the acquisition of an asset or a group of assets might involve the use of hindsight in determining the acquisition-date fair values of the identifiable assets acquired and of the liabilities assumed as part of the business combination transaction. It also noted that the amendment is only a clarification of the interrelationship between IFRS 3 and IAS 40. Consequently, it decided that an entity would apply the amendments to IAS 40 prospectively for annual periods beginning on or after 1 July 2014 but that retrospective application of that amendment should be permitted but only if information needed is available to the entity.