

Welcome to the IFRIC Update

IFRIC Update is the newsletter of the IFRS Interpretations Committee (the 'Interpretations Committee'). All conclusions reported are tentative and may be changed or modified at future Interpretations Committee meetings.

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

The Interpretations Committee met in London on **14 July 2015**, when it discussed:

■ Item on the current agenda:

- IFRS 11 *Joint Arrangements*—Should a pre-existing interest in a joint operation be remeasured when the entity becomes a joint operator through acquisition of an additional interest in the joint operation? (Agenda Paper 6)

■ Deliberation of comments received on proposals for narrow scope amendments

- IFRS 2 *Share-based Payment*—Clarification and measurement of share based payment transactions (Agenda Papers 2 and 2A)

■ Item recommended to the IASB for Annual Improvements

- IAS 23 *Borrowing Costs*—Borrowing costs on completed qualifying assets (Agenda Paper 7)

■ Interpretations Committee tentative agenda decisions

- IAS 2 *Inventories* / IAS 38 *Intangible Assets*—Should interest be accreted on prepayments in long-term supply contracts? (Agenda Paper 3)
- IAS 12 *Income Taxes*—Recognition through profit or loss of deferred taxes for temporary differences arising from the effect of exchange rate changes on the tax basis of non-current assets (Agenda Paper 9)

■ Other matters

- Interpretations Committee work in progress update (Agenda Papers 10 and 10A)
- Review of IFRS Interpretations Committee's activity during January–May 2015 (Agenda Paper 10B)

■ Interpretations Committee agenda decision

- IFRIC 14 *IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*: Should an entity assume continuation of a minimum funding requirement for contributions relating to future service?

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:
8 and 9 September 2015
10 and 11 November 2015

Meeting dates, tentative agendas and additional details about the next meeting will be posted to the IASB [website](#) before the meeting. Further information about the activities of the IFRS Interpretations Committee can be found [here](#). Instructions for submitting requests for Interpretations are given on the IASB website [here](#).

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Item on the current agenda

At this meeting, the Interpretations Committee discussed the following item on its current agenda.

IFRS 11 Joint Arrangements—Should a pre-existing interest in a joint operation be remeasured when the entity becomes a joint operator through acquisition of an additional interest in the joint operation? (Agenda Paper 6)

The Interpretations Committee received a request to clarify whether a previously held interest in the assets and liabilities of a joint operation is remeasured to fair value when the investor's acquisition of an additional interest results in the investor becoming a joint operator (ie obtaining joint control) in the joint operation.

At this meeting the Interpretations Committee discussed an analysis of other transactions involving changes of interests in a business (as defined by IFRS 3 *Business Combinations*) for which there is a lack of guidance, or where there is diversity of views, on determining whether or not previously held interests should be remeasured. The analysis identified 14 such transactions. The analysis indicated that several of these transactions were either not widespread, not resulting in diversity in practice or were the subject of another IASB project. On the basis of the analysis, the Interpretations Committee agreed that the scope of the project, initially, should include transactions involving:

- a. obtaining control of a joint operation, either from having joint control in a joint operation or being a party to a joint operation prior to the transaction;
- b. loss of control resulting in the entity having joint control in a joint operation or being a party to a joint operation subsequent to the transaction; and
- c. change of interests resulting in a party to a joint operation obtaining joint control in a joint operation.

The Interpretations Committee observed that it would be useful to also analyse similar transactions involving assets, or groups of assets and liabilities, that do not meet the definition of a business.

The Interpretations Committee asked the staff to prepare a paper that analyses the accounting for previously held interests for the transactions identified, taking into account existing principles that can be carried over to these transactions. It also expressed a preference that any guidance that might be developed as part of this work should be informed by the other IASB projects referred to, and should consider the implications on the accounting for other similar transactions.

The staff will present this further analysis at a future meeting.

Deliberation of comments received on proposals for narrow-scope amendments

IFRS 2 Share-based payment—Exposure Draft *Clarification and Measurement of Share-based Payment Transactions* (Proposed amendments to IFRS 2) (Agenda Papers 2 and 2A)

In November 2014 the IASB published for comment the Exposure Draft *Clarification and Measurement of Share-based Payment Transactions* (Proposed amendments to IFRS 2). The comment period ended on 25 March 2015.

This Exposure Draft exposed together three separate proposed amendments to IFRS 2 *Share-based Payment*. These three issues are:

- a. effects of vesting conditions on the measurement of a cash-settled share-based payment;
- b. classification of share-based payment transactions with net settlement features; and
- c. accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

At this meeting, the Interpretations Committee was presented with a summary and an analysis of the 70 comment letters received on the Exposure Draft.

Most respondents broadly support the proposals. They think that the proposed amendments provide practical solutions and reduce the risk of diversity in practice in the application of IFRS 2.

However, some respondents requested further clarification or simplification of the proposed amendments. A majority of respondents agreed with the proposed prospective application of the amendments but requested further guidance for the transition and application of the proposed amendments to new awards and existing unvested awards.

The Interpretations Committee decided to propose that the IASB should finalise the proposed amendments, subject to some revisions to the proposed wording.

With respect to the proposed amendments about the *effects of vesting conditions on the measurement of a cash-settled share-based payment* the Interpretations Committee decided to propose to the IASB that it should:

- a. include some wording changes in paragraphs 19 and 33 of IFRS 2 to clarify that the impact of market and non-vesting conditions should not be taken into account when adjusting the number of instruments included in the measurement of a share-based payment transaction; and
- b. indicate that the guidance in paragraphs 30–33C of IFRS 2 for measuring the liability incurred should be applied to all cash-settled awards and that share appreciation rights are an example of cash-settled share based payment transactions.

With respect to the proposed amendments about the *classification of share-based payment transactions with net settlement features* the Interpretations Committee decided to propose to the IASB that it should:

- a. modify the heading before paragraph 33D to indicate that the proposed exception applies to a limited type of award with net settlement features (as described in paragraph 33D).
- b. retain the existing scope of the proposed exception to require the transaction to be classified as equity-settled in its entirety and reinforce the reasons in the Basis for Conclusions why the proposed classification represents an exception to the requirements in IFRS 2.
- c. add Example 12B to the implementation guidance in IFRS 2 to illustrate the accounting for the transaction with net settlement features described in paragraph 33D.
- d. require that the cash paid to the tax authority should be accounted for in accordance with paragraph 29 of IFRS 2 (ie as a deduction from equity, but with any amount paid in excess of the fair value of the shares withheld being recognised as an expense in profit or loss); and that any excess of the fair value of the shares withheld over the tax liability should be accounted for as a cash-settled share-based payment if that excess is paid as cash to the employee. The Interpretations Committee further proposed to the IASB that an entity should disclose information about the estimated amount of cash that the entity will need to pay in connection with the withholding of the employee's tax obligation on the share-based payment transaction.

With respect to the proposed amendments about the *accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled* the Interpretations Committee decided to propose to the IASB that it should:

- a. include in the Basis for Conclusions a reference to paragraph 3.3.3 of IFRS 9 *Financial Instruments* and paragraph 9 of IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* to reinforce the reasons why the difference between the liability derecognised and the amount of equity recorded at the modification date should be recognised in profit or loss;
- b. add Example 12C to the implementation guidance in IFRS 2 to illustrate a modification of the terms and conditions of a cash-settled share-based payment that results in a change in the classification of the share-based payment transaction from cash-settled to equity-settled as a result of issuing replacement awards; and
- c. specify in paragraph B41A of IFRS 2 that a change in classification from a cash-settled award to an equity-settled award can occur during or outside the vesting period and that when the vesting period is extended or shortened, an entity should recognise any difference between the cash-settled award (recognised as a liability) and the amount of the equity-settled award (recognised in equity) immediately in profit or loss for the accrued portion of each award by reference to the modified vesting period.

With respect to the transition guidance for the proposed amendments, the Interpretations Committee decided to propose to the IASB that it should explain how the three proposed amendments should be applied for new awards and for outstanding unvested awards:

- a. for modifications that change the classification from cash-settled to equity-settled, the proposed amendments should apply to modifications that occur after the date that the amendments are first applied.
- b. for existing unvested cash-settled awards that are subject to vesting and non-vesting conditions, an entity should adjust the carrying amount of the liability in the statement of financial position in the period of change on the date that the amendments are first applied. The entity should recognise the effect of the change, ie any cumulative catch-up adjustment, in equity (ie retained earnings or another appropriate component of equity) at the beginning of the annual period in which the amendments are first applied.
- c. for awards with net settlement features that meet the criteria for the exception in paragraph 33D, at the date that the amendments are first applied an entity should assess any existing unvested arrangements with such net settlement features that have been classified as cash-settled or that have been classified using a 'bifurcation' approach (ie in accordance with paragraph 34 of IFRS 2). If the entity concludes that such arrangements should be classified as equity-settled in accordance with the amendments, the entity should reclassify the current carrying value of the liability to equity. This adjustment is recognised in equity (ie retained earnings or another appropriate component of equity) at the beginning of the period in which the amendments are first applied.

The staff will present the Interpretations Committee's recommendations at a future IASB meeting.

Item recommended to the IASB for Annual Improvements

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

IAS 23 Borrowing Costs—Borrowing costs on completed qualifying assets (Agenda Paper 7)

The Interpretations Committee received a request seeking clarification on whether funds borrowed specifically to finance the construction of a qualifying asset, the construction of which has now been completed, must be included as part of general borrowings for the purposes of determining the capitalisation rate for other qualifying assets under IAS 23 *Borrowing Costs*.

At its May 2015 meeting, a majority of the Interpretations Committee tentatively agreed that, on the basis of the wording in paragraph 14 of IAS 23, the specific borrowings should be included within general borrowings in the fact pattern described by the submitter. However, the Interpretations Committee noted that there is diversity in practice, which arises from a perceived lack of clarity in the wording in paragraph 14 of IAS 23. The Interpretations Committee tentatively decided that the wording in IAS 23 should be clarified through an annual improvement.

At its meeting in July 2015, the Interpretations Committee agreed with the principle of the proposed amendment to paragraph 14 of IAS 23; however, it noted that the proposed wording for the amendment in the Staff Paper should be amended to make it clear that all borrowings, other than those for which borrowing costs are capitalised in accordance with paragraph 12 of IAS 23, should be included in the general borrowings pool.

The Interpretations Committee agreed that the proposed amendment met the criteria for Annual Improvements and that it should be applied prospectively.

The staff will present the proposed annual improvement to the IASB at a future meeting.

Interpretations Committee tentative agenda decisions

The Interpretations Committee reviewed the following matters and tentatively decided that they should not be added to its agenda. These tentative decisions, including recommended reasons for not adding the items to the Interpretations Committee's agenda, will be reconsidered at the Interpretations Committee meeting in November 2015. Interested parties who disagree with the proposed reasons, or believe that the explanations may contribute to divergent practices, are encouraged to email those concerns by 28 September 2015 to ifric@ifrs.org. Correspondence will be placed on the public record unless the writer requests confidentiality, supported by good reason, such as commercial confidence.

IAS 2 Inventories and IAS 38 Intangible Assets—Should interest be accreted on prepayments in long-term supply contracts? (Agenda Paper 3)

The Interpretations Committee received a request seeking clarification on the accounting for long-term supply contracts of raw materials when the purchaser of the raw materials agrees to make significant prepayments to the supplier. The question considered is whether the purchaser should accrete interest on long-term prepayments by recognising interest income, resulting in an increase in the cost of inventories and, ultimately, the cost of sales.

The Interpretations Committee discussed this issue and noted that paragraph 18 of IAS 2 *Inventories* requires that when an entity purchases inventories on deferred settlement terms, and the arrangement contains a financing element, the difference between the purchase price on normal credit terms and the amount paid is recognised separately as interest expense over the period of the financing. It also noted that IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* include similar requirements when payment for an asset is deferred. IFRS 15 *Revenue from Contracts with Customers*, issued in May 2014, additionally includes the requirement that the financing component of a transaction should be recognised separately in circumstances of both prepayment and deferral of payment.

The Interpretations Committee conducted outreach on this issue, but the outreach returned very limited results. In the absence of evidence about this issue, and of a broader range of information about the facts and circumstances relating to these transactions, the Interpretations Committee thought it would be difficult for it to address this topic efficiently and effectively. The Interpretations Committee observed, however, that when a financing component is identified in a long-term supply contract of raw materials, that financing component should be accounted for separately. The Interpretations Committee acknowledged that judgement is required to identify when individual arrangements contain a financing component.

The Interpretations Committee concluded that this issue did not meet its agenda criteria and therefore it [decided] to remove this issue from its agenda.

IAS 12 Income Taxes—Recognition through profit or loss of deferred taxes for temporary differences arising from the effect of exchange rate changes on the tax basis of non-current assets (Agenda Paper 9)

The Interpretations Committee received a submission regarding the recognition of deferred taxes when the tax bases of an entity's non-monetary assets and liabilities are determined in a currency that is different from its functional currency. The question is whether deferred taxes arising due to the effect of exchange rate changes on the tax bases of non-current assets are recognised through profit or loss.

The Interpretations Committee noted that, in relation to the fact pattern analysed, paragraph 41 of IAS 12 *Income Taxes* states that when an entity's tax base of a non-monetary asset or liability is determined in a currency that is different from the functional currency, temporary differences arise resulting in a deferred tax asset or liability. Such deferred tax does not arise from a transaction or event that is recognised outside profit or loss and is therefore charged or credited to profit or loss in accordance with paragraph 58 of IAS 12. Such deferred tax charge or credit would be presented with other deferred taxes, instead of with foreign exchange gains or losses, in the statement of profit or loss.

The Interpretations Committee also noted that paragraph 79 of IAS 12 requires the disclosure of the major components of tax expense (income). The Interpretations Committee observed that when changes in the exchange rate are the cause of a major component of the deferred tax charge or credit,

an explanation of this in accordance with paragraph 79 of IAS 12 would help explain the tax expense (income) to the users of the financial statements.

In the light of the existing IFRS requirements the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary and therefore [decided] not to add this issue to its agenda.

Other matters

Interpretations Committee work in progress update (Agenda Papers 10 and 10A)

The Interpretations Committee received a report about ongoing issues that were not discussed at this meeting. Specifically, the Interpretations Committee received a status update, by a separate paper, on the issue on classification of liability for prepaid cards issued by a bank in the bank's financial statements.

Review of IFRS Interpretations Committee's activity during January–May 2015 (Agenda Paper 10B)

The Interpretations Committee received a report on the number and types of activities undertaken over the last half year and how those activities have been evolving. This report included a summary of its activities during the last half year and a comparison with respect to previous years.

Interpretations Committee agenda decision

The following explanations are published for information only and do not change existing IFRS requirements. Interpretations Committee agenda decisions are not IFRIC Interpretations. IFRIC Interpretations are determined only after extensive deliberations and due process, including a formal vote, and become final only when approved by the IASB.

IFRIC 14 IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction: Should an entity assume continuation of a minimum funding requirement for contributions relating to future service?

The Interpretations Committee received a request to clarify whether the future minimum funding requirement for contributions to a defined benefit plan to cover future service would apply for only the fixed period that had been agreed between the entity and the pension trustees. The conclusion on this issue could affect how the economic benefit available as a reduction in future contributions is determined, which could in turn affect the amount of the net defined benefit liability or asset to be recognised in the entity's statement of financial position.

In the circumstances described by the submitter, neither a plan wind-up nor a plan closure to future accrual has been decided upon at the end of the reporting period. In addition, a pension regulation or a contractual agreement, or both, specify that:

- a. the pension trustees are required to prepare, and from time to time review and if necessary revise, a statement of funding principles that documents the pension trustees' policy for ensuring that a required funding objective is met;
- b. the statement of funding principles sets out, among other things, the methods to be used to determine the assumptions that are used to calculate the liabilities that determine contributions to be paid;
- c. the pension trustees are required to prepare a schedule of contributions that is negotiated with the entity and that is consistent with the statement of funding principles;
- d. the amounts specified in the schedule of contributions must then be paid for a fixed period;
- e. the entity and the pension trustees are required to renew the schedule of contributions as the fixed period comes to an end if the plan is continued;
- f. the schedule of contributions does not need to be renewed if the plan is wound up; and
- g. the entity can decide to wind up or close the plan to future accrual, if this is agreed with the pension trustees.

The Interpretations Committee observed that, although the level of contributions after the fixed period

will be subject to future negotiations, if the plan continues after the fixed period the entity must continue to make contributions for future service that are consistent with the statement of funding principles.

The Interpretations Committee noted that paragraph 18 of IFRIC 14 requires an entity to analyse its minimum funding requirements at a given date into the contributions that are required to cover:

- a. any existing shortfall for past service on the minimum funding basis; and
- b. future service.

The Interpretations Committee also noted that:

- a. paragraph 19 of IFRIC 14 explains that contributions to cover any existing shortfall for past service do not affect future contributions for future service; and
- b. paragraph 23 of IFRIC 14 requires an entity to determine whether contributions payable to cover an existing shortfall for past service will be available as a refund or reduction in future contributions.

The Interpretations Committee noted that the question raised by the submitter relates only to the minimum funding requirement for contributions to cover future service.

The Interpretations Committee then noted that, in the circumstances described, the pension trustees determine some or all of the factors (or funding principles) establishing the minimum funding basis (as that term is used in IFRIC 14) and record them in the statement of funding principles. Accordingly, when the entity estimates the future minimum funding requirement contributions, it should (i) include the amounts in the schedule of contributions for the fixed period specified by the schedule; and (ii) beyond that period, make an estimate that assumes a continuation of those factors establishing the minimum funding basis as determined by the pension trustees. This is because:

- a. paragraphs 21 and BC30 of IFRIC 14 explain that an entity's estimate of future minimum funding requirement contributions shall not include the effect of expected changes in the terms and conditions of the minimum funding basis that are not substantively enacted or contractually agreed at the end of the reporting period; and
- b. in the circumstances described, those factors establishing the minimum funding basis that are determined by the pension trustees and recorded in the statement of funding principles are equivalent to a legal requirement or contractual agreement. Accordingly, the estimate of future minimum funding requirement contributions for future service should not assume any changes to those factors if such changes require future negotiations with the pension trustees.

The Interpretations Committee further noted that, for any factors affecting the estimation of future minimum funding requirements that are not determined by the trustees (for example, the remaining life of the plan is not specified by the existing funding principles), the assumptions used to estimate future minimum funding requirement contributions for future service beyond the fixed period must be consistent with those used for determining future service costs. This is because paragraphs 17 and 21 of IFRIC 14 require an entity to use assumptions that are consistent with those used to determine the defined benefit obligation and with the situation that exists at the end of the reporting period.

On the basis of this analysis, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary and therefore decided not to add this issue to its agenda.

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