

Beyond the GAAP

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Just a few days apart in May, the IASB and FASB published their jointly developed proposals on presentation of items contained in Other Comprehensive Income (OCI). However, these proposals could be seen as something of a smokescreen... What is the point of ensuring comparability in terms of presentation of items of OCI if the use of this category, in particular for recognition of financial instruments, differs from one set of standards to another? The FASB's simultaneous publication of an exposure draft on financial instruments seems to announce a short-term failure for convergence... Otherwise, what will be the price of convergence?

Enjoy your reading!

Michel Barbet-Massin

Jean-Louis Lebrun

Editorial

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News

Appointments to the IFRS Interpretations Committee (formerly the IFRIC)

On 4 May, the IFRS Foundation (International Financial Reporting Standards Foundation) announced a number of new and renewed appointments to the IFRS Interpretations Committee, formerly the IFRIC.

Placing the emphasis on continuity at a time of extensive revision of IFRSs, the IFRS Foundation has reappointed Robert Garnett as chairman of the Interpretations Committee for a further two-year period from 1 July 2010, despite his retirement as a member of the IASB on 30 June.

Three members with expiring terms have been reappointed as members of the Committee for a further three year term with effect from 1 July 2010: Guido Fladt (PwC), Bernd Hacker (formerly of Siemens) and Andrew Vials (KPMG).

Finally, Feilong Li, controller of CNOOC, China's largest offshore crude oil and natural gas producer with a dual-listing in Hong Kong and the United States, has been appointed for a three-year term as a member of the Interpretations Committee. He replaces Darrel Scott (FirstRand Banking Group), who has been appointed to serve as a member of the IASB from October 2010.

IFRS News

➤ The IASB publishes an exposure draft on the presentation of Other Comprehensive Income (OCI)

On 27 May, the IASB published an exposure draft on the presentation of items of Other Comprehensive Income (OCI). The FASB published a similar document the day before, at the same time as the exposure draft on financial instruments (see below). The increased use of the OCI category in the FASB's draft standard on financial instruments may explain this timing.

As suggested in the March 2010 edition of *Beyond the GAAP*, the main proposal in the IASB's exposure draft is the removal of the current option to present comprehensive income in two separate statements (one of which is the statement of profit or loss). This option will be replaced by a single statement. This statement, which the exposure draft calls the "Statement of profit or loss and other comprehensive income" (replacing the "Statement of comprehensive income" but these titles would continue not to be mandatory) would nevertheless continue to present two distinct sections, profit or loss followed by items of other comprehensive income, with the total comprehensive income at the foot of the statement.

The exposure draft also proposes to require that items of OCI that will never be recognised in profit or loss should be presented separately from those that are subject to subsequent reclassification.

Note: one question in the exposure draft asks commentators for their response to the Board's assessment of the benefits and costs of its proposals. Evidence that the IASB is anxious to be seen to be listening to the concerns of preparers in particular; concerns that were widely expressed during the call for comments on the discussion paper "Presentation of Financial Statements" in 2009.

Finally, it may be helpful to stress that the IASB states that it has no plans to eliminate profit or loss as a measure of performance. Profit or loss will still be presented separately and will remain the required starting point for the calculation of earnings per share.

The IASB staff have prepared a list of 10 Q&A to assist understanding of the aims and impacts of the proposals in the exposure draft.

This document, and the exposure draft itself, can be accessed on the IASB website page presenting the project:

<http://www.iasb.org/News/Press+Releases/improvements+to+OCI.htm>

Comments may be submitted until 30 September 2010. The final standard should be available by the end of the year.

➤ Publication of the exposure draft on measurement of financial liabilities

On 11 May the IASB published an exposure draft on measurement of financial liabilities. This exposure draft completes phase 1 of the project to replace IAS 39 on financial instruments.

This exposure draft proposes to maintain the existing provisions of IAS 39 on financial liabilities, with one exception regarding fair value option. Financial liabilities will continue to see changes in value from one period to the next recognised in profit or loss. However, the portion of the change in fair value due to the issuer's own credit risk element would be reversed out of profit or loss and recognised in other comprehensive income. The amounts thus transferred in OCI would not subsequently be recycled to profit or loss.

This proposal represents the only amendment to the existing provisions of IAS 39, as is reflected in the title of the exposure draft itself, "Fair value option for financial liabilities".

The Board thus proposes to take a different approach to classification and measurement of financial assets and liabilities.

By way of example, we can mention the retention of the notion of embedded derivatives for financial liabilities, and the divergent ways of taking into account the entity's business model (a condition affecting the classification of assets at amortised cost and the classification of liabilities as held for trading).

Comments on the exposure draft should be submitted by 16 July 2010.

➤ The FASB publishes its exposure draft on financial instruments

On 26 May 2010, the FASB published its exposure draft on "Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities".

This project, developed in parallel to the replacement of IAS 39, but in collaboration with the IASB, is part of the process of convergence between the two sets of standards.

The exposure draft covers all aspects of financial instruments (measurement, impairment and hedge accounting) with the exception of derecognition issues.

Despite the proposed convergence, a number of divergences have already been identified. For example:

- the FASB proposes to measure all financial assets at fair value, while the IASB favours a mixed approach combining amortised cost and fair value. However, the FASB proposes to present the amortised cost of some assets in the statement of financial position in the form of a fair value sub-total;
- unlike the IASB, the FASB proposes to measure financial assets and financial liabilities in the same way (embedded derivatives are eliminated from both sides), though allowing an "amortised cost option" for some liabilities for which fair value measurement would result in accounting mismatches (e.g. financial liabilities backed by operating assets measured at cost).

Beyond the GAAP will return in more detail to this exposure draft and the divergences between it and the IASB proposals once the IASB will have presented all its proposed amendments to IAS 39 (an exposure draft on hedging is expected during the second quarter).

Comments on the FASB exposure draft should be submitted by 30 September 2010.

➤ Partial disposal of an interest in an associate or a joint venture

During discussions on the future standard on joint arrangements at its May meeting, the IASB decided that, when an entity is committed to a sale plan involving loss of significant influence of an associate or loss of joint control of a jointly controlled entity, only the portion of the interest that will be disposed of should be presented as "held for sale", provided that all the criteria of IFRS 5 are met.

The retained interest will continue to be recognised in accordance with the equity method (the only method authorised for joint arrangements in the standard that will replace IAS 31) until the disposal.

This decision thus completely overturns the approach suggested in the August 2009 exposure draft on annual improvements (see Beyond the GAAP No 32 - March 2010).

➤ Leases: derecognition model for lessor accounting

At their joint meeting of May 2010, the IASB and the FASB discussed lessor accounting issues and the two possible approaches:

- The performance obligation approach (which had previously been preferred); and
- The derecognition approach.

The two Boards first confirmed that, under the performance obligation approach, the lessor has a single performance obligation to continue to permit the lessee to use the leased asset over the lease term. The asset continues to be recognised in the lessor's financial statements. A receivable is recognised to offset the liability (the performance obligation). The performance obligation is satisfied (and thus revenue is recognised) continuously over the lease term.

As decided at the joint meeting of April 2010, the two Boards then discussed the derecognition approach, and opted for a partial derecognition approach under which the lessor:

- derecognises the portion of the underlying asset corresponding to the right of use granted to the lessee over the lease term, measured as the present value of the rents receivable;
- retains in his statement of financial position the residual asset representing its right to the underlying asset at the end of the lease period. This residual asset is initially measured on the basis of an allocation of the previous carrying amount of the underlying asset. The residual asset would not be remeasured unless for impairment;
- recognises the revenue for the disposal of the right of use at the time the asset is delivered against the rents receivable. If the lessor is also the manufacturer of the underlying asset, it immediately recognises its margin on the construction.

When concluding this May session, a large majority of FASB members indicated that they would prefer the performance obligation approach for all types of lessors.

Conversely, a large majority of IASB members declared a preference for a hybrid approach under which some lessors (for instance, manufacturers or dealers) would apply the partial derecognition approach and others would use the performance obligation method. The IASB will shortly discuss the criteria for distinguishing these two types of lessors.

It should be remembered that the future standard on leases will exclude from its scope leases that are, in substance, sales/purchases (see Beyond the GAAP No 31 February 2010). For lessors that are manufacturers or dealers, leases that are currently similar to in substance sales should therefore not be affected by the choice between the performance obligation approach and the partial derecognition approach.

➤ Puts on non-controlling interests

At the meeting of 6 and 7 May 2010, the IFRS Interpretations Committee (ex IFRIC) considered a question on subsequent changes in the liability for a put option on non-controlling interests. Given the potential conflict between IAS 32 (which refers back to IAS 39) and IAS 27R, two approaches can be taken :

- the first approach consists of recognising all subsequent changes in the fair value of the liability in profit or loss;
- the second approach is based on the general requirements of IAS 27R for the purchase of non-controlling interests. This approach leads to the recognition of changes in the carrying amount of the liability (the put) in equity.

At the end of its discussions, the Interpretations Committee decided that, given the diversity in practice related to this issue, it would add the project to its agenda, without expressing any preference for either approach at this stage. It should be noted that, in 2006, the IFRIC decided not to address this topic.

Beyond the GAAP will keep you up to date with the progress of these discussions.

European Matters

➔ IFRS for SMEs: what do the stakeholders think in Europe?

In May, the European Commission published a report following the consultations on IFRS for SMEs that ended on 12 March 2010.

More than 200 comment letters have been received, mostly from preparers (41%) and accountants and auditors (33%). All EU Member States expressed their views, with Germany particularly well represented.

The arguments in favour of the IFRS for SMEs mainly relate to greater harmonisation and the improved comparability of SMEs' financial statements. The adoption of this standard would make it easier to attract foreign investors and thus reduce the cost of capital. For international groups, reconciliations in order to standardise accounting principles in subsidiaries in different countries would no longer be necessary.

The arguments against the IFRS for SMEs mainly relate to the complexity and the cost of implementing this standard, especially for the smallest entities. It is of limited value, for example, to companies operating in local markets and with a small shareholdership. Finally, the connection between taxation and accounting in many States poses a problem.

A majority of commentators wanted the legal framework for accounting in Europe to include the option to adopt

the IFRS for SMEs. The possibility of offering this option in each Member State, rather than at entity level, also attracted support.

In 2008, the EU launched a programme for the modernisation and simplification of the accounting directives. The IASB's publication in July 2009 of the IFRS for SMEs has encouraged the Commission to include this area in its own deliberations.

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IASB's annual omnibus of Improvements to IFRSs

On 6 May 2010, the IASB published its annual omnibus on Improvements to IFRSs.

Of the 15 proposed amendments exposed for public comments in August 2009, 10 were finalised and an additional amendment to IFRS 1 (First-time Adoption of IFRSs) applicable to entities with operations subject to rate regulated activities was included. The 5 proposed amendments excluded from the Annual Improvements Project (AIP) are listed in a table together with the reasons for their exclusion at the end of the article.

➤ Main amendments

IFRS 1 – First-time Adoption of IFRSs – Changes in accounting policies in the year of adoption

This amendment provides clarification as to what happens for first-time adopters changing policies between their first interim financial statements presented in accordance with IAS 34 and their first presented IFRS annual financial statements. Constituents' views were mixed as to whether IAS 8 should apply under these specific circumstances. The amendment therefore clarifies that IAS 8 does not apply in such circumstances. However, the reconciliations required by IFRS 1 with previous GAAP need be updated.

IFRS 1 – First-time Adoption of IFRSs – Revaluation basis as deemed cost

Before this amendment, the use of the revaluated amount as deemed cost was possible if the revaluation occurred before the entity's date of transition to IFRSs.

However, in some jurisdictions (eg in China), the local law requires revaluation to fair value of an entity's assets and liabilities, for example in case of an Initial Public Offering (IPO). When such an IPO occurs just after the date of transition to IFRSs, an entity following the previous requirements in IFRS 1 would have had to prepare two sets of measurements for its assets and liabilities, one to comply with IFRS, and one to comply with the local law.

The amendment aims to allow an entity to recognise an event-driven fair value measurement as deemed cost when the event occurs, provided that this is during the periods covered by its first IFRS financial statements. Thus, an entity shall recognise the resulting adjustments directly in retained earnings at the measurement date.

In addition, in response to comments received, the IASB decided to expand the exemption to entities that adopted IFRSs in any period before the amendment is effective (i.e. whether they adopted IFRSs using IFRS 1 or formerly SIC-8).

IFRS 1 – First-time Adoption of IFRSs – Use of deemed cost for operations subject to rate-regulation

Thanks to this amendment, entities operating in rate-regulated environments and adopting IFRSs for the first time are permitted to use, at the date of transition, the carrying amounts of items of property, plant and equipment (PP&E) or intangible assets used for rate-regulated operations under the previous GAAP. This exemption applies item by item.

Therefore, under the previous GAAP, an entity may have included in the cost of PP&E items that were not recognisable under IFRSs, e.g. an allowance from the regulator for the cost of financing the acquisition of an item of PP&E. Such items could be maintained at the transition date, even though IFRSs would not permit to capitalise them.

In addition, in the specific circumstances of operations in rate-regulated environments, using the fair value of PP&E as deemed cost in accordance with the existing exemption in IFRS 1 raises practical issues as entities do not have readily available fair value information for these PP&E or intangible items.

IFRS 3 – Business Combinations – Transition requirements for contingent consideration from a business combination that occurred before the effective date of the revised IFRS

IFRS 3 as revised in 2008 requires that contingent consideration:

- be measured at fair value at the acquisition date with subsequent changes through profit or loss (ie no subsequent impact on the consideration transferred and goodwill), and
- be within the scope of IAS 39/IFRS 9 if it meets the definition of a financial instrument.

Concerns were expressed that, for contingent consideration related to business combinations that occurred prior to the application of IFRS 3R, these requirements were contradictory to the transitional requirements of IFRS 3R. In accordance with these requirements, assets and liabilities from such business combinations should remain accounted for in accordance with previous IFRS 3 (as issued in 2004).

To address these concerns, the amendment clarifies that subsequent contingent consideration that relate to business combinations prior to the application of IFRS 3R should be treated as an adjustment to the cost of the business combination when they become probable and can be measured reliably.

Accordingly, the amendment modifies IAS 39 to specify that that standard does not apply to contingent consideration from business combinations that occurred prior to the application of IFRS 3R.

IFRS 3 – Business Combinations – Measurement of non-controlling interests

IFRS 3R changed the terminology and the definition of 'minority interest' to 'non-controlling interest' (NCI). The current definition of non-controlling interest, being all interest not held by the parent, includes items that would not have met the definition of minority interest. This is the case for example for share-based payment transactions classified as equity or for the equity component of a convertible bond.

Before its revision, IFRS 3 required that NCI could be measured either at fair value or at the NCI's proportionate share of the acquiree's identifiable net assets. Thus, the equity component of a convertible bond could be measured at the proportionate share of the NCI's identifiable net assets in the acquiree, ie. at a nil value because such equity component does not entitle to a proportionate share of the acquiree's identifiable net assets in the event of liquidation.

The amendment aims to limit the measurement of the proportionate share of the acquiree's identifiable net assets that only applies to non-controlling interest that are currently entitled to a proportionate share of the acquiree's net assets in the event of liquidation. Other non-controlling interests are measured at fair value or as required by relevant IFRSs.

IFRS 3 – Business Combinations – Un-replaced and voluntarily replaced share-based payment awards

Before the amendment, IFRS 3R addressed the accounting for acquiree's share-based payment transactions (awards) that the acquirer is obliged to replace in the context of a business combination. The standard provides guidance on the portion of the 'market-based measure' of the awards that should be included in the consideration transferred - i.e. the portion of the acquiree's awards attributable to pre-combination employees' services.

The IASB acknowledged that there was a lack of guidance on the accounting for voluntarily replacements. The amendment clarifies that such voluntarily replacement should follow the same accounting requirements as those the acquirer is obliged to replace. Therefore, for voluntarily replacements, if acquiree awards do not expire as a consequence of a business combination, a portion of the replaced awards reflects the acquiree's obligation that remains outstanding at the date of the business combination and should therefore be included in the consideration transferred.

In addition, the amendment provides guidance for a circumstance in which the acquiree awards expire as a consequence of the business combination but are voluntarily replaced by the acquirer. In that circumstance, replaced awards should be considered entirely as post-combination costs (the cost of the business combination is not affected). This is because the new awards granted by the acquirer do not result from an obligation to the employees (with respect to past services that they provided to the acquiree before the business combination).

IFRIC 13 – Customer Loyalty Programmes – Fair value of award credits

The amendment clarifies guidance on measuring award credits, especially in the light of the new definition of fair value introduced by the forthcoming Fair Value Measurement standard. Practically, measurement of the award credits is based on the retail sales price adjusted for discounts that would be offered to customers who have not earned award credits from an initial sale, and for expected forfeitures.

➔ Other amendments

IFRS	Subject of the amendment
IFRS 7 – <i>Financial Instruments: Disclosures</i>	Clarifies disclosures about the nature and extent of risks arising from financial instruments
IAS 1 – <i>Presentation of Financial Statements</i>	Clarifies that beginning/end of period reconciliations for changes resulting from other comprehensive income for each component of equity can be either detailed in the notes to or in the Statement of Changes in Equity.
IAS 27 – <i>Consolidated and Separate Financial Statements</i>	Clarifies that amendments to IAS 21, IAS 28 et IAS 31 arising from the revision of IAS 27 in 2008 apply prospectively.
IAS 34 – <i>Interim Financial Reporting</i>	<p>Confirms the general principles that information disclosed in interim financial reporting, when an entity publishes a set of condensed financial statements, should update the relevant information presented in the most recent annual financial report when significant to an understanding of the changes in financial position and performance of the entity.</p> <p>This amendment gives a list of events or transactions that occurred during the interim period and that shall be disclosed if the information is significant. That list is linked with certain information required under IFRS 7.</p>

➤ Effective date and transition

These amendments shall be applied on or after:

- 1 July 2010 for amendments to IFRS 3R and amendments arising as a result of IAS 27 (2008) apply prospectively, and
- 1 January 2011 for the others, with retrospective application in accordance with IAS 8.

➤ Proposed amendments excluded from the 2008-2010 AIP cycle

For further details on these former proposals, please refer to Beyond the GAAP published in October 2009.

IFRS	Subject of proposed amendment	Reasons for exclusion from the 2008-2010 AIP cycle
IFRS 5 – <i>Non-current Assets Held for Sale and Discontinued Operations</i>	Application to loss of significant influence over an associate or loss of joint control in a jointly controlled entity.	In February 2010, the Board decided to retain the term “significant economic event” for the event of loss of control only. This decision is inconsistent with the rationale for the amendment to IFRS 5 as proposed that relied on the economic similarity of the events. The issue was analysed again as part of the Joint Arrangements project (for more details see the highlights, page 3).
IAS 8 – <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	Change in terminology to the qualitative characteristics.	Publication was pending the relevant chapters of the forthcoming Conceptual Framework being issued before the publication of the <i>Improvements to IFRSs</i> . Sweep issues in the Conceptual Framework project delayed publication; hence the amendment to IAS 8 was not included in the <i>Improvements to IFRSs</i> issued in May 2010.

IFRS	Subject of proposed amendment	Reasons for exclusion from the 2008-2010 AIP cycle
IAS 27 – <i>Consolidated and Separate Financial Statements</i>	Impairment of investments in subsidiaries, jointly controlled entities and associates in the separate financial statements of the investor.	Comments received in respect of the appropriate impairment model were split fairly evenly between responses in favour of the use of IAS 39 and responses in favour of the use of IAS 36. The Board decided to address this issue as part of the broad IAS 39 replacement project rather than on a piecemeal basis.
IAS 28 – <i>Investments in Associates</i>	Partial use of fair value for measurement of associates.	Given that the forthcoming standard on <i>Joint Arrangements</i> will have consequential amendments to IAS 28, the Board decided to include this amendment as part of the consequential amendments to IAS 28.
IAS 40 – <i>Investment Property</i>	Change from fair value model to cost model.	Comments received were mainly in favour of addressing the issue as part of a standalone project after reviewing interactions with other standards (e.g. IFRS 5, IAS 16). The IFRS Interpretations Committee will discuss this issue soon in order to make proposals to the Board.

➤ And now, make way for the annual improvements for 2009-2011!

During May and June 2010, the IASB will publish a large number of exposure drafts. Preparers, users and auditors will have some pressure to submit their comments within the deadlines. In this context, the next exposure draft on annual improvements will not be issued before October 2010, with a view to publishing the definitive omnibus as originally planned in May 2011.

What impact will IFRS 3R have on business combinations that occurred in or after 2010?

Our April edition presented the impact of the new standards IFRS 3R and IAS 27R at the transition date (i.e. 1 January 2010 in the case of entities with a reporting date at the end of December that had not opted for early application). We now return to the main changes introduced by IFRS 3R for new business combinations.

For a reminder of the main changes introduced by the publication of IFRS 3R and IAS 27R, see our Mazars Insight: "Business combinations and consolidation – Key points of the new standards in 40 questions and answers".

Our next edition will return to the main impacts of the new IAS 27R, in particular on the accounting treatment of changes in the interest held in subsidiaries, whether or not leading to loss of control.

Apart from the extension of its scope, the main impacts of the application of IFRS 3R relate to the amendments and clarifications that the standard brings to aspects of the acquisition-related costs, and the identification and measurement of the identifiable assets and liabilities acquired.

It should be remembered that the scope of IFRS 3R now includes operations involving mutual entities, but it still excludes the formation of joint ventures and business combinations under common control.

➤ Determination of the consideration transferred

Note that the standard refers to "consideration transferred" or price paid, but "cost of the business combination" is still widely used.

The main changes introduced by IFRS 3R to the determination of the "cost of the business combination" relate to the following aspects:

- the costs associated with the combination are now recognised as expenses (instead of being included in the cost of the business combination);
- an interest previously held is remeasured at the date control is obtained and recognised in profit or loss (as if the interest had been disposed of before being immediately re-acquired), whereas the remeasurement in equity under the previous version of the standard was linked to the method of calculating goodwill;
- it is possible, for each business combination, to measure non-controlling interests either at fair value ("full goodwill" method introduced by the revised standard), or at the proportionate share of the acquiree's identifiable net assets ("Partial goodwill");

The IFRS Improvements published on 6 May 2010 clarifies that this choice only applies to the shares in the acquiree held by third parties.

The other elements classified in the acquiree's equity (i.e. other elements of non-controlling interests, such as purchase options issued by the acquiree, or the conversion option component of a bond) must be measured at fair value (or on the basis of other applicable IFRS) when control is obtained (ie the acquisition date).

- contingent consideration must be measured at fair value on the acquisition date, even if the payment is not probable (before IFRS 3R, contingent consideration was only included in the acquisition costs if the payment was probable and it was possible to measure the amount reliably).

Therefore, goodwill is determined once and for all at the acquisition date (a single goodwill amount replacing the previous tranches determined on the acquisition of additional interests).

Adjustments to contingent consideration only affect goodwill if (a) they take place during the allocation period (a maximum of 12 months from the acquisition date), if (b) they are analysed as paid in cash and if (c) the adjustment results from new information obtained after the acquisition date about facts and circumstances that existed at the acquisition date.

In the general case of contingent consideration paid in cash, changes in estimates after the allocation period would be recognised in profit or loss (whereas contingent consideration was offset against goodwill without time limits in the former version of IFRS 3).

The same conclusion applies in the event of contingent consideration paid with the acquirer's shares when the transaction is not an equity transaction under IAS 32 (for example when the number of shares delivered is variable, i.e. when the acquirer's shares are used as a payment method).

➤ Elements included in the cost of the business combination

As well as introducing a number of amendments, IFRS 3R also provides clarification regarding the elements of the acquisition costs.

Thus, the fact that the consideration transferred to the seller is legally linked to the acquisition of the acquiree's shares by the acquirer does not necessarily imply that, for accounting purposes, this consideration should be analysed in its entirety as representing the price paid for the shares.

It may be necessary, for instance, to separate the part of the consideration transferred that represents the price of the shares from the part that remunerates something else.

It is therefore important to have a thorough understanding of the economics of the transaction, including the reasons for the transaction (i.e. does it principally benefit the acquirer or the acquiree and the acquiree's former shareholders?), who initiated the transaction (understanding who initiated the transaction may help identify which elements are part of the business combination), and the timing of the transaction.

The standard provides some examples, such as the settlement of a 'pre-existing relationship' between the acquirer and the acquiree, the replacement of the acquiree's share-based payments awards by the acquirer, and contingent payments made to the sellers for their continuing employment in the acquiree.

Where there exist commercial relationships between the acquirer and the acquiree (for example, a supply contract or the right to use a trademark), it will be necessary to distinguish in the price paid the amount actually paid for the

acquisition of shares and the element which relates to the settlement of a pre-existing relationship.

The acquirer must recognise a gain or loss on the settlement of a pre-existing relationship, measured in accordance with the nature of the relationship (contractual, e.g. a supply contract, or non-contractual, e.g. processes).

Furthermore, when the acquirer had granted the acquiree a right (e.g. the right to use a trademark), the acquirer must recognise an asset measured on the basis of the residual term of the contract (i.e. without taking into account potential renewals).

When the acquiree's share-based payments awards are replaced by the acquirer's similar awards, IFRS 3R states that it is necessary to determine what element in the replacement awards that represents part of the consideration transferred, and what is remuneration for post-combination service.

The IFRS Improvements published on 6 May 2010, no longer make a distinction on the basis of whether or not the acquirer is under an obligation to replace the acquiree awards.

Finally, in the event that the sellers continue to work in the acquired company, the standard states that payments made to the sellers must be analysed to determine whether:

- these payments represent part of the consideration transferred (e.g. an earn-out clause), or
- these payments instead remunerate a service (to be recognised in expenses if the former shareholders provide services as employees).

The standard provides several indicators for use in the analysis. By way of an exception, when payments are no longer due because the employee has left the company, the payments must be treated as relating to post-combination services (i.e. personnel expenses).

➤ Identification and measurement of assets acquired and liabilities assumed

The main amendments and clarifications introduced by IFRS 3R to the identification and measurement of assets acquired and liabilities assumed are as follows:

- intangible assets can always be reliably measured, uncertain cash flows being integrated into the fair value measurement (the previous version allowed entities not to recognise an intangible asset if its fair value could not be reliably measured);
- fair value is independent of the intentions of the acquirer (the acquirer may intend not to use an asset, or to use it in a way that is different from the use that a market participant would use it);
- the fair value of an asset must be considered as a new gross value;
- the classification of assets and liabilities should normally be carried out on the basis of the conditions existing at the date of the business combinations (exception: the classification of leases and insurance contracts is based on the original contract conditions, unless these conditions have been modified);
- the favourable or unfavourable nature (relative to market conditions) of an operating lease will give rise to the recognition of an intangible asset or a liability in the lessee's financial statements (and is taken into account as a component of the fair value of the asset in the lessor's financial statements) ;

- re-acquired rights (such as the right to use a trademark or a patent previously granted by the acquirer to the acquiree) must be measured on the basis of their residual contractual term (and amortised over the same period);
- contingent liabilities recognised in a business combination now only include present obligations that can be measured reliably and for which an outflow of economic resources is not probable (before IFRS 3R, contingent liabilities comprised both possible obligations whose existence will be confirmed by the occurrence of future events and present obligations) ;

The exposure draft "Measurement of liabilities in IAS 37" published in January 2010 by the IASB also proposes to recognise present obligations for which an outflow of economic resources is not probable (see question no 22 in the study in the January 2010 edition of Beyond the GAAP).

- the seller's guarantees on any assets or liabilities give rise to the recognition of an asset (indemnification asset) in the acquirer's financial statements. This indemnification asset is measured on the same basis as the liability that is guaranteed (i.e. consistency of both initial and subsequent assumptions, taking into account any risk of non-recovery).

The revised standard does not change the measurement period during which the acquirer must finalise the business combinations (i.e. the maximum allocation period remains twelve months from the acquisition date). However, the transitional amounts recognised at the acquisition date can only be adjusted to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised at that date.

Furthermore, and contrary to the former version of the standard, there is no longer an exception for deferred tax assets recognised by the acquiree after the allocation period (i.e. they are still recognised in profit or loss, but with no corresponding goodwill adjustment).

What amendments to IAS 19 are suggested (ED/2010/3)?

In April 2010, the IASB published for comment the exposure draft ED/2010/3 proposing a number of changes to IAS 19. Comments may be submitted until 6 September 2010.

The proposed amendments cover the following areas:

- The immediate recognition of any changes in the obligation or in the value of the plan assets, aiming to improve the clarity of the presentation of the financial statements in these respects and to make them more readily comparable, removing the option of the 'corridor' for the recognition of actuarial gains and losses;
- the revision of the presentation of the different components of these changes;
- the improvement of disclosures, with the addition of information about the risks arising from these plans.

The exposure drafts brings clarification to certain issues brought to light during the response phase to the 2008 discussion paper, in particular in respect of:

- the classification of some benefits;
- measurement ;
- the tax treatment applicable to some plans.

Finally, the exposure draft proposes to integrate IFRIC 14, "IAS 19 – The limit of a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" in the standard.

A significant feature of the proposals is the amalgamation of the categories "post-employment benefits" and "other long term benefits" into a single category entitled "long-term benefits": the proposals of the exposure draft have therefore an impact on long-term benefits, in particular in relation to the recognition of actuarial gains and losses and the disclosures to be provided in the notes.

➤ Immediate recognition of changes in obligations or the value of plan assets

The exposure draft identifies three major disadvantages in the current accounting treatment of actuarial gains and losses and the costs of unvested past services:

- The deferred recognition of some elements can lead to an inappropriate presentation in the balance sheet, an asset being recognised when the plan in question is in deficit;
- the fact that some elements can be recognised in different ways leads to the recognition over one period of an amount arising from an event that occurred in a past period;
- the existence of options for the recognition of actuarial gains and losses makes a comparison of financial statements more complex.

The proposal of the exposure draft, i.e. the immediate recognition of any changes in the obligation or the value of the plan assets, aims to remove these weaknesses from the standard, at the price of an increased volatility of the statement of financial position.

➤ Presentation of changes in the obligation and in the value of plan assets

The exposure draft proposes to divide changes in the obligation and the value of plan assets into three components:

- service cost, to which would be added gains and losses from curtailment of the plan, in profit or loss:

Service cost combines the cost of services rendered for the period with the cost of past services, whether vested or otherwise, resulting from a change or an introduction of a plan for the period.

- net interest on the net asset or liability, calculated on the basis of the discount rate of the liability, as a part of the finance costs in profit or loss;
- the impact of remeasuring the asset or the liability recognised in other comprehensive income without the option to recycle in profit or loss:

Remeasurement of liabilities include the effect of a settlement, whether the remeasurement is linked to the exercise of an option as part of the plan regulations or caused by an event (in any case, the exposure draft analyses this type of effect as experience adjustments).

➤ Improving the disclosures

The exposure draft proposes to supplement the information in the notes with:

- a narrative discussion about risk exposure, both in terms of the obligations under the plan and of the plan assets;
- greater details on the actuarial gains and losses generated, distinguishing the impact of changes in demographic assumptions from that of changes in financial assumptions;
- more disclosures on the actuarial assumptions, and on the way they are determined;

However, the exposure draft does not precise which assumptions should be subject to disclosure. Entities would exercise their judgment in assessing which assumptions are material.

- information about the obligation, excluding the impact of future increases;

This information increases transparency in cases where the plan in question is closed, and thus makes it possible to meet the expectations of those stakeholders who were in favour of not taking into account future increases in the obligation at the time of responses to the 2008 discussion paper.

- information on the uncertainties of future cash flows, in particular via:
 - a sensitivity analysis of the significant assumptions, and a description of the methodology used in preparing this analysis;
 - details of any asset-liability matching strategies and the use by the plan, including the use of annuities and other techniques;
 - a narrative discussion of the factors likely to affect the level of the contributions over the next five years and the period over which it expects the surplus or deficit to disappear.

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Events/publications

Seminars on "Current developments in IFRS"

Mazars' Technical Department will host a number of seminars throughout 2010 dedicated to current developments in IFRS. These seminars, organised by Francis Lefèbvre Formation, will be held 25 June, 24 September and 10 December 2010.

To register, please contact Francis Lefèbvre Formation – www.flf.fr, +33 (0)1 44 01 39 99.

Frequently asked questions

IAS/IFRS

- Accounting treatment of the restructuring of a liability and impact on hedging;
- Possibility of carrying out a basis adjustment in a cash flow hedge of a highly probable future transaction for the acquisition of an associate;
- Presentation of information about operating segments in the case of a matrix form of organisation;
- Review of foreign currency hedging contracts;
- Business combination under IFRS 3R: single operation or step acquisition?

Upcoming meetings of the IASB, IFRIC and EFRAG

IASB

14 - 18 June 2010

19 - 23 July 2010

13 - 17 September 2010

IFRIC

8 - 9 July 2010

2 - 3 September 2010

4 - 5 November 2010

EFRAG

9 - 11 June 2010

14 - 16 July 2010

8 - 10 September 2010

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