Raymond Chabot Grant Thornton

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IFRS Newsletter

August 2014

Welcome to *IFRS Newsletter* – a newsletter that offers a summary of certain developments in International Financial Reporting Standards (IFRS) along with insights into topical issues.

In this August 2014 edition, we will cover new standards issued by the International Accounting Standards Board (IASB), Exposure Drafts issued, IFRS-related news at Grant Thornton and a general round-up of financial reporting developments.

You can find out about the implementation dates of newer standards, some of them being not yet mandatory towards the end of this document, as well as a list of IASB publications that are out for comment.

IASB completes IFRS 9 *Financial Instruments (2014)*

The IASB has finished its project to replace *IAS 39 Financial Instruments: Recognition and Measurement* (IAS 39) by publishing IFRS 9 (2014).

The IASB began its overhaul of the accounting for financial instruments in the summer of 2009 in response to the widespread criticism of IAS 39 and its alleged role in contributing to the financial crisis of 2007-2008. In order to allow for a phased completion of the standard, IFRS 9 was divided into chapters with the first chapter being published in 2009. The publication of IFRS 9 (2014) completes these chapters and therefore the standard as a whole.

Changes made by IFRS 9 (2014)

IFRS 9 (2014):

- adds requirements dealing with expected credit losses (impairment);
- amends the classification and measurement requirements by adding a new measurement category for financial assets;
- introduces a new mandatory effective date.

Expected credit losses

IFRS 9 (2014) contains the requirements on expected credit losses. IAS 39's impairment requirements had been criticized for being overly complicated and resulting in impairment being recognized at too late a stage. IFRS 9 (2014) addresses these criticisms by applying the same impairment model to all financial assets that are subject to impairment accounting and by using more forward-looking information. In applying this more forward-looking approach, a distinction is made between:

- financial assets that have not deteriorated significantly in credit quality since initial recognition or that have low credit risk and;
- financial assets that have deteriorated significantly in credit quality since initial recognition and whose credit risk is not low.

"Twelve-month expected credit losses" are recognized for the first category while "lifetime expected credit losses" are recognized for the second category. There is also a third step to the model in the sense that for assets which actually become credit-impaired after initial recognition, interest is calculated on the asset's amortized cost (i.e. the amount net of the loss allowance) as opposed to its gross carrying amount.

Amendments to the classification and measurement requirements

IFRS 9 (2014) introduces a new measurement category of fair value through other comprehensive income for financial assets. An entity must classify a financial asset in this new category if both of the following conditions are met:

- The financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

New mandatory effective date

IFRS 9 (2014) introduces a new mandatory effective date of annual periods beginning on or after January 1, 2018.

Extensive transition provisions have been included due to the complexity of the requirements and the phased way in which the project has been completed.

Grant Thornton International comment

IFRS 9 (2014) is likely to result in significant changes to many entities' financial statements. While its effective date of 2018 may seem a long way off, we strongly advise companies to start evaluating the new standard now as it may have important ramifications in terms of system requirements and ratios.

A special edition of *IFRS Newsletter* on IFRS 9 (2014) will be issued in the near future which will cover the requirements of the standard in more depth and prepare you for the changes.

IASB amends IFRS 11

The IASB has published *Accounting for Acquisitions of Interests in Joint Operations* (Amendments to IFRS 11), providing guidance on the accounting for the acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business.

Grant Thornton International comment

We welcome the Amendments to IFRS 11. Prior to its publication, the initial accounting for an interest in a joint operation was not adequately addressed by IFRS 11. We therefore welcome the Amendments, which we believe will serve to reduce the existing diversity in practice in the accounting for such transactions.

More specifically, the Amendments to IFRS 11 *Joint Arrangements* state that an acquirer of an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3 *Business Combinations*, should:

- apply all of the principles on business combinations accounting in IFRS 3 and other IFRS apart from principles that conflict with the guidance of IFRS 11. This requirement also applies to the acquisition of additional interests in an existing joint operation and to the acquisition of an interest in a joint operation on its formation;
- provide disclosures for business combinations as required by IFRS 3 and other IFRS.

Additionally, consequential amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards* have been made so that IFRS 1's exemption for past business combinations can also apply to past acquisitions of interests in joint operations in which the activity of the joint operation constitutes a business.

The Amendments to IFRS 11 are to be applied prospectively for annual periods beginning on or after January 1, 2016, with earlier application permitted.

The Amendments to IFRS 11 are to be applied prospectively for annual periods beginning on or after January 1, 2016, with earlier application permitted.

IASB amends IAS 16 and IAS 38

The IASB has published *Clarification of Acceptable Methods of Depreciation and Amortization* (Amendments to IAS 16 and IAS 38) in order to address depreciation and amortization methods which are based on revenue.

The Amendments to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* stem from concerns regarding the use of a revenue-based method for depreciating an asset. By way of background, the two standards require that a depreciation or amortization method should reflect the expected pattern of consumption of the future economic benefits of the asset. The Amendments result from a request to clarify the meaning of the term "consumption of the expected future economic benefits of the asset".

Grant Thornton International comment

We welcome the Amendments to IAS 16 and IAS 38. While we agree that a depreciation and amortization method based on revenue is generally inappropriate, we believe that for some intangible assets the expected future pattern of revenue could serve as a valid proxy for the expected consumption of economic benefits in particular circumstances. We therefore support the changes made by the IASB.

The Amendments to IAS 16

The Amendments to IAS 16 prohibit the use of a revenue-based depreciation method for property, plant and equipment because:

- a depreciation method which is based on revenue allocates the asset's depreciable amount based on revenue generated in an accounting period as a proportion of total expected revenue during the asset's useful life;
- revenue reflects a pattern of economic benefits that are generated from operating the business rather than the economic benefits that are being consumed through use of the asset.

The Amendments to IAS 38

The Amendments to IAS 38 present a rebuttable presumption that a revenue-based amortization method for intangible assets is inappropriate for the same reasons set out above. This rebuttable presumption can be overcome, i.e. a revenue-based amortization method might be appropriate, only in two limited circumstances:

1. The intangible asset is expressed as a measure of revenue, for example when the predominant limiting factor inherent in an intangible asset is the achievement of a revenue threshold; or
2. When it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.

Application of the diminishing balance method

In addition, the IASB has taken the opportunity to expand on the guidance on applying the diminishing balance method to property, plant and equipment and to intangible assets.

Effective date and transition

The Amendments should be applied prospectively for annual periods beginning on or after January 1, 2016. Earlier application is permitted.

New accounting for bearer plants

The IASB has published *Agriculture: Bearer Plants – Amendments to IAS 16 and IAS 41* (the Amendments), changing the accounting for a subset of biological assets known as bearer plants.

Grant Thornton International comment

We welcome the Amendments which will reduce the cost, complexity and practical difficulties of measuring bearer plants at fair value less costs to sell in the absence of markets for these assets. At the same time, the Amendments will enable the accounting to better reflect the economic nature of these plants as productive assets.

IAS 41 *Agriculture* requires all biological assets that are related to agricultural activity to be measured at fair value less costs to sell (subject to fair value being reliably measurable), based on the principle that their biological transformation is best reflected by fair value measurement. However, there is a class of biological assets, known as bearer plants, that, once mature, are held by an entity solely to grow produce over their productive life. Examples include grape vines, rubber trees and oil palms.

Constituents told the IASB that IAS 41's fair value model was not appropriate for mature bearer plants that are no longer undergoing significant biological transformation as the way they use these assets is more similar in nature to manufacturing. The IASB has listened to these concerns and made changes to IAS 16 and IAS 41. The Amendments:

- add a definition of "bearer plants" (which is not met if there is a more than "remote" likelihood that the plant will be sold as agricultural produce, incidental scrap sales excepted);
- include bearer plants within the scope of IAS 16 instead of IAS 41 (produce growing on bearer plants remains within the scope of IAS 41);
- clarify that until bearer plants are mature, they are to be accounted for as self-constructed items of property, plant and equipment;
- require any difference between fair value and the carrying amount under IAS 41 (fair value less costs to sell) at the time of initial adoption to be recognized in opening retained earnings;
- exempt entities from the requirement in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* to disclose the impact of initial application on each financial statement line item affected;
- permit the fair value of the bearer plants at the beginning of the earliest period presented to be used as the deemed cost for IAS 16 purposes when first applied.

The Amendments do not result in any changes to existing accounting for "bearer livestock" or plants with more than a remote likelihood of being harvested and sold as agricultural produce.

The Amendments are effective for annual periods beginning on or after January 1, 2016 with earlier application permitted.

IASB proposes to clarify the consolidation exception for investment entities

The IASB has published the Exposure Draft *Investment Entities–Applying the Consolidation Exception (Proposed amendments to IFRS 10 and IAS 28)*.

The Exposure Draft proposes amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures*, addressing three issues which had been submitted to the IFRS Interpretations Committee (IFRIC) related to the implementation of the consolidation exception for investment entities.

Issue	Principal considerations	Proposal
Exemption from preparing consolidated financial statements	IFRS 10.4(a) provides an exemption from presenting consolidated financial statements for a parent entity that meets specified criteria. One of these criteria is that its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRS.	The Exposure Draft proposes to amend IFRS 10 to confirm that the exemption in IFRS 10.4(a) continues to be available to a parent entity that is a subsidiary of an investment entity, even when the investment entity measures its subsidiaries at fair value in accordance with IFRS 10.31.
A subsidiary that provides services that relate to the parent's investment activities	In a situation where a subsidiary of an investment entity itself meets the definition of an investment entity and in addition provides services that relate to the parent's investment activities, it was unclear whether the investment entity parent should measure the subsidiary at fair value or consolidate it.	The Exposure Draft proposes that the requirement for an investment entity to consolidate a subsidiary, instead of measuring it at fair value, applies only to those subsidiaries that act as an extension of the operations of the investment entity parent, and do not themselves qualify as investment entities. The main purpose of such a subsidiary is to provide support services that relate to the investment entity's investment activities (which may include providing investment-related services to third parties).
Application of the equity method by a non-investment entity investor to an investment entity investee	IFRS 10.33 states that a non-investment entity parent of an investment entity cannot retain the fair value measurement applied by the investment entity to its interests in subsidiaries and must therefore consolidate all subsidiaries in the group. However, there was no equivalent explicit statement related to the application of the equity method by a non-investment entity investor for its investments in joint ventures or associates that are investment entities.	The IASB proposes to amend IAS 28 to: • provide relief to a non-investment entity investor by requiring it to retain, when applying the equity method, the fair value measurement applied by an investment entity associate to its interests in subsidiaries; and • clarify that a non-investment entity investor that is a joint venturer in a joint venture that is an investment entity cannot, when applying the equity method, retain the fair value measurement applied by the investment entity joint venture to its interests in subsidiaries.

Equity method in separate financial statements

The IASB has published *Equity Method in Separate Financial Statements* (Amendments to IAS 27) containing narrow-scope amendments to IAS 27 *Separate Financial Statements.*

Grant Thornton International comment

The inclusion of the equity method as one of the options to account for an entity's investments in subsidiaries, joint ventures and associates in the entity's separate financial statements should come to reduce the burdens on entities in some jurisdictions and encourage greater use of IFRS.

While we acknowledge that there are some concerns with the Amendments in that they will reduce consistency and lack a clear conceptual basis, we support them on pragmatic grounds.

Prior to the publication of the Amendments to IAS 27, IAS 27 required an entity to account for its investments in subsidiaries, joint ventures and associates either at cost or in accordance with IFRS 9 (or IAS 39 where an entity has not yet adopted IFRS 9).

In response to the IASB's 2011 Agenda Consultation, some of the IASB's constituents noted however that:

- the laws of some countries require listed companies to present separate financial statements prepared in accordance with local regulations;
- those local regulations require the use of the equity method to account for investments in subsidiaries, joint ventures and associates;
- in most cases, the use of the equity method would be the only difference between the separate financial statements prepared in accordance with IFRS and those prepared in accordance with local regulations.

As a result, the IASB has published the Amendments to IAS 27, introducing a third option which would allow entities to account for investments in subsidiaries, joint ventures and associates under the equity method. Entities will have an accounting policy choice in their separate financial statements between accounting:

- at cost;
- in accordance with IFRS 9 (or IAS 39);
- under the equity method.

Entities are required to apply the same accounting for each category of investments. The Amendments are effective for annual periods beginning on or after January 1, 2016. Earlier application is permitted. No transitional provisions have been included as the IASB believes entities should be able to use information that is already available to them in applying the Amendments.

IFRS 15: A new global standard on accounting for revenue

As mentioned in our last edition of *IFRS Newsletter*, the IASB published IFRS 15 *Revenue from Contracts with Customers*, the product of a major joint project between the IASB and the U.S. Financial Accounting Standards Board (FASB).

For more information about the new standard, please refer to our June 2014 *IFRS Newsletter – Special Edition on Revenue*.

To supplement the *IFRS Newsletter – Special Edition on Revenue*, in the coming months we intend to provide industry-specific insights.

Grant Thornton International comment

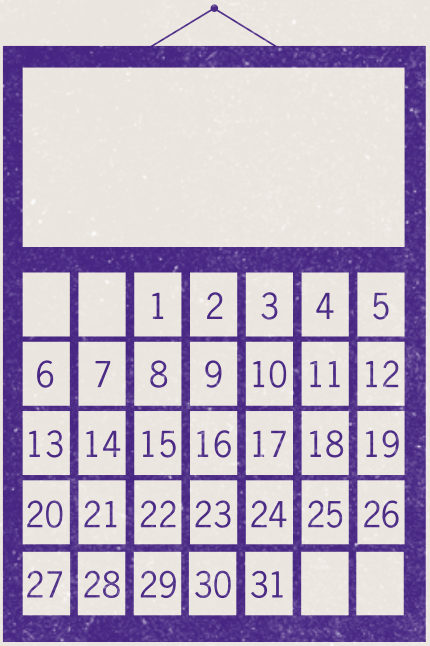
We applaud the IASB and the FASB for delivering a converged standard on this critical area of accounting. We see this as a landmark achievement that will provide a major boost for investors looking to compare performance across borders.

The impact on the top line will very much depend on each company's specific customer contracts and how the much less detailed existing standards have been applied. For some it will be a significant shift while others may see only minor changes. Companies are advised to start their assessment of IFRS 15 now in order to determine which camp they fall into.

IASB and FASB form Joint Transition Resource Group for Revenue Recognition

The IASB and FASB have announced the formation of a Joint Transition Resource Group for Revenue Recognition (TRG).

The TRG will inform the IASB and the FASB about potential implementation issues that could arise when companies and organizations implement the new standard. The TRG will also provide stakeholders with an opportunity to learn about the new standard from others involved with implementation. The TRG will not issue guidance.



Spotlight on our IFRS Interpretations Group

Grant Thornton International's IFRS Interpretations Group (IIG) consists of a representative from each of our member firms in the United States, Canada, Singapore, Australia, South Africa, India, the United Kingdom, Ireland, France, Sweden and Germany as well as members of the Grant Thornton International IFRS team. The Group meets in person twice a year to discuss technical matters which are related to IFRS.

In each newsletter, we throw a spotlight on one of the members of the IIG. In this newsletter, we focus on the representative from Australia:

Andrew Newman, Australia

Andrew has worked with Grant Thornton for the past 15 years spending time in both the Brisbane, Australia and the New York offices. Andrew is currently an audit partner in the Brisbane office. His client base is across the public, private and not-for-profit space in sectors including technology and media, manufacturing, retail, resources, financial services and real estate and construction industries. While predominately working on external audit engagements, Andrew is also involved in internal audit engagements and acts as an expert witness on accounting standard and audit matters. He also facilitates training sessions on accounting standards and financial reporting for CPA Australia.

Rinna Sak appointed as member of the IFRS Discussion Group

Rinna Sak, National Director of Accounting Standards and Partner at Grant Thornton LLP, has been appointed as a member of the IFRS Discussion Group (IDG) for an initial three-year term.

As Grant Thornton's National Director of Accounting Standards, Rinna oversees or participates in all important initiatives related to IFRS, including assessing complex and judgmental accounting and reporting issues for clients and professional staff, educating accounting professionals and external audiences and performing quality reviews.

The IDG was established by the Canadian Accounting Standards Board (AcSB) to implement and maintain a regular public forum to discuss issues that arise in Canada when applying IFRS. While the IDG's discussions are not authoritative, the IDG is well-respected in the accounting standard-setting community, both in Canada and globally.

Round-up

Disclosure Initiative update

The IASB has published an update on its *Disclosure Initiative* (a portfolio of projects designed to improve the quality of information provided in financial reports).

In its update, the IASB notes that it has been hearing concerns that its plans for developing disclosure principles and replacing IAS 1 *Presentation of Financial Statements*, IAS 7 *Statement of Cash Flows* and IAS 8 will not bring improvements quickly enough. It is therefore looking to accelerate the development of a Discussion Paper in this area.

The IASB's update also notes that as part of its work on materiality, it is developing proposals designed to help entities determine which of their accounting policies are "significant". It is also reviewing how materiality is defined, interpreted and applied in different jurisdictions and for different purposes related to financial reporting including securities law, auditing standards and local generally accepted accounting principles (GAAP).

Updated IASB work plan

Following on from its July meeting, the IASB has updated its work plan. The new work plan lists the following standards as due for publication in the third quarter of 2014:

- *Annual improvements – 2012-2014 cycle*;
- *Sale or contribution of assets between an investor and its associate or joint venture* (Amendments to IFRS 10 and IAS 18).

IASB to establish transition resource group for impairment of financial instruments

The IASB has announced its intention to create a transition resource group that will focus on the new requirements for impairment of financial instruments. The group will provide a discussion forum to support stakeholders on implementation issues that may arise as a result of the new impairment requirements under IFRS 9 *Financial Instruments (2014)*, which were issued in the third quarter of 2014.

The group will solicit, analyze and discuss common stakeholder issues arising from implementation of the new requirements that could possibly create diversity in practice. It will also provide information that will help the IASB determine what, if any, action will be needed to resolve such diversity. The group will not issue guidance itself however.

ESMA report on business combinations

The European Securities and Markets Authority (ESMA) has published a report entitled *Review on the application of accounting requirements for business combinations in IFRS financial statements*. The report finds that some good business combination disclosures are provided in the annual financial statements of European companies but that there are also certain areas where improvements are needed.

In its report, ESMA urges companies to provide disclosures tailored to the specific circumstances of their transactions. In particular, ESMA believes companies could further improve the quality of information relating to business combinations by:

- providing relevant information about the factors determining the amount of goodwill or reasons for bargain purchases;
- providing more granular disclosures on the assets and liabilities recognized, where relevant;
- applying consistent assumptions at the initial recognition and subsequent measurement of assets and liabilities;
- improving the information provided on the valuation techniques and assumptions used when measuring assets and liabilities at fair value.

IASB agrees charter of mutual co-operation with accounting standard-setting community

The IASB has published an updated charter establishing key principles of co-operation between the IASB and national standard-setters and other accounting standard-setting bodies. The principles established by the charter are designed to enhance the efficiency and effectiveness of international accounting standard-setting. The charter:

- emphasizes the importance of the global accounting standard-setting community to the work of the IASB and builds on the premise that it is essential that all parties should work together in a spirit of openness and close co-operation in order to meet shared goals;
- describes a shared understanding of the commitments and expectations of the IASB and national standard-setters and other accounting standard-setting bodies, presented as a statement of co-operation;
- focuses on practical aspects whereby staff and members of the IASB and other accounting standard-setters can work co-operatively, describing the actions and procedural matters that deserve the most care.

Effective dates of new standards and IFRIC interpretations

The table below lists new IFRS Standards and IFRIC Interpretations with an effective date on or after January 1, 2013. Companies are required to make certain disclosures in respect of new Standards and Interpretations under IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

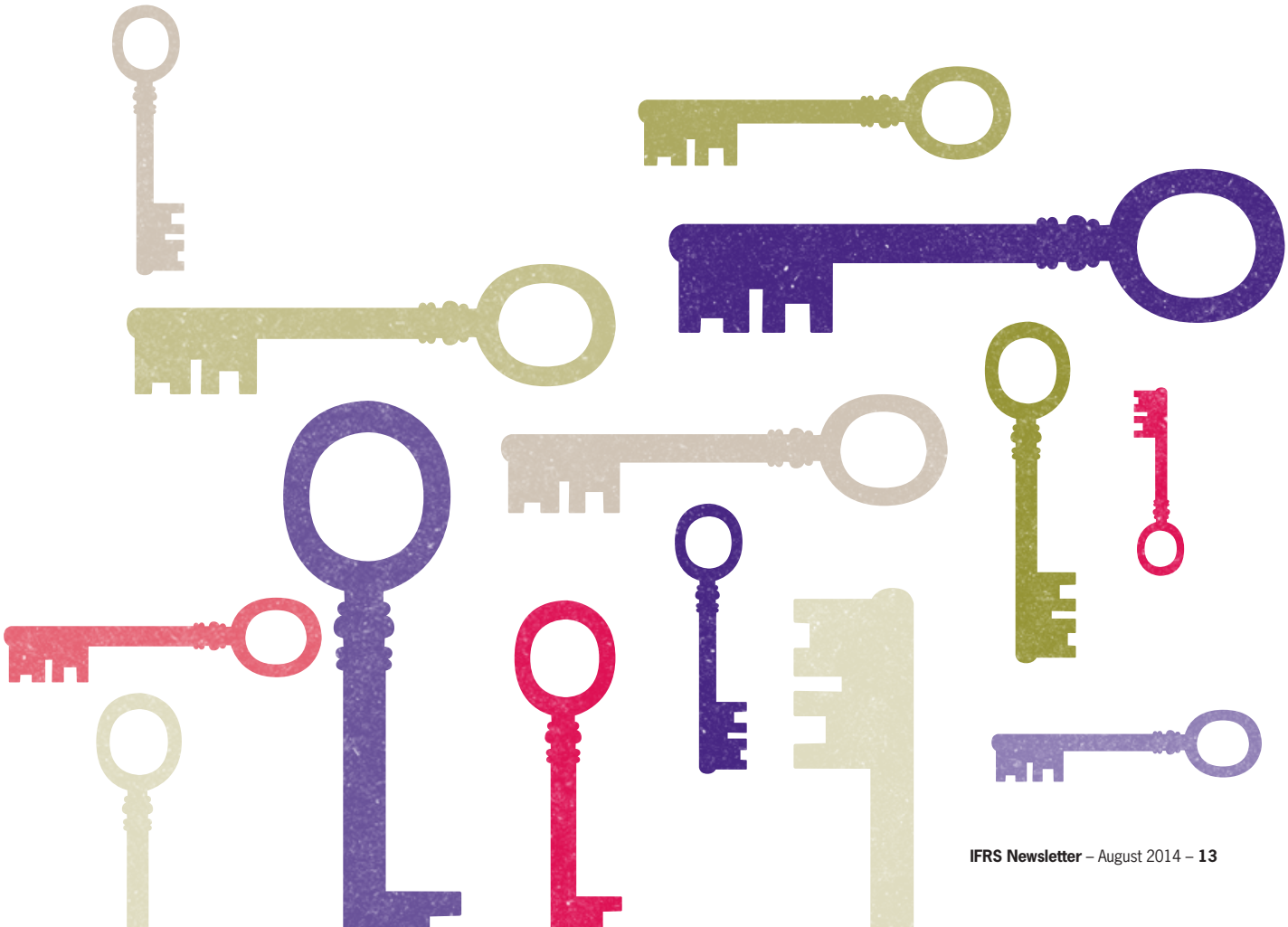
New IFRS standards and IFRIC interpretations with an effective date on or after January 1, 2013

Title	Full title of standard or interpretation	Effective for accounting periods beginning on or after	Early adoption permitted?*
IFRS 9	*Financial Instruments*	January 1, 2018	Yes (extensive transitional rules apply)
IFRS 15	*Revenue from Contracts with Customers*	January 1, 2017	Yes
IAS 27	*Equity Method in Separate Financial Statements*	January 1, 2016	Yes
IAS 16 and IAS 38	*Clarification of Acceptable Methods of Depreciation and Amortization* (Amendments to IAS 16 and IAS 38)	January 1, 2016	Yes
IFRS 11	*Accounting for Acquisitions of Interests in Joint Operations* (Amendments to IFRS 11)	January 1, 2016	Yes
IFRS 14	*Regulatory Deferral Accounts*	January 1, 2016	Yes
IAS 19	*Defined Benefit Plans: Employee Contributions* (Amendments to IAS 19)	July 1, 2014	Yes
Various	*Annual Improvements to IFRS 2011-2013 Cycle*	July 1, 2014	Yes
Various	*Annual Improvements to IFRS 2010-2012 Cycle*	July 1, 2014	Yes
IAS 39	*Novation of Derivatives and Continuation of Hedge Accounting* (Amendments to IAS 39)	January 1, 2014	Yes
IAS 36	*Recoverable Amount Disclosures for Non-Financial Assets* (Amendments to IAS 36)	January 1, 2014	Yes (but only when IFRS 13 is applied)
IFRIC 21	*Levies*	January 1, 2014	Yes
IFRS 10, 12 and IAS 27	*Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27)	January 1, 2014	Yes
IAS 32	*Offsetting Financial Assets and Financial Liabilities* (Amendments to IAS 32)	January 1, 2014	Yes (but must also make the disclosures required by *Disclosures – Offsetting Financial Assets and Financial Liabilities*)
IFRS 10, 11 and 12	*Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance* (Amendments to IFRS 10, IFRS 11 and IFRS 12)	January 1, 2013	Yes
Various	*Annual Improvements to IFRS 2009-2011 Cycle*	January 1, 2013	Yes

New IFRS standards and IFRIC interpretations with an effective date on or after January 1, 2013

Title	Full title of standard or interpretation	Effective for accounting periods beginning on or after	Early adoption permitted?*
IFRS 1	*Government Loans* (Amendments to IFRS 1)	January 1, 2013	Yes
IFRS 7	*Disclosures – Offsetting Financial Assets and Financial Liabilities* (Amendments to IFRS 7)	January 1, 2013	Not stated (but we presume yes)
IFRIC 20	*Stripping Costs in the Production Phase of a Surface Mine*	January 1, 2013	Yes
IFRS 13	*Fair Value Measurement*	January 1, 2013	Yes
IFRS 12	*Disclosure of Interests in Other Entities*	January 1, 2013	Yes
IFRS 11	*Joint Arrangements*	January 1, 2013	Yes (but must apply IFRS 10, IFRS 12, IAS 27 and IAS 28 at the same time)
IFRS 10	*Consolidated Financial Statements*	January 1, 2013	Yes (but must apply IFRS 11, IFRS 12, IAS 27 and IAS 28 at the same time)
IAS 28	*Investments in Associates and Joint Ventures*	January 1, 2013	Yes (but must apply IFRS 10, IFRS 11, IFRS 12 and IAS 27 at the same time)
IAS 27	*Separate Financial Statements*	January 1, 2013	Yes (but must apply IFRS 10, IFRS 11, IFRS 12 and IAS 28 at the same time)
IAS 19	*Employee Benefits (Revised 2011)*	January 1, 2013	Yes
IFRS Practice Statement	*Management Commentary: A framework for presentation*	No effective date as non-mandatory guidance	Not applicable

* As a note of caution, to be in accordance with Canadian GAAP and securities regulations, an entity may not early adopt a new or amended IFRS until its issuance by the Chartered Professional Accountants of Canada (CPA Canada) in the *CPA Canada Handbook – Accounting*.



Open for comment

This table lists the documents that the IASB currently has out for comment and the comment deadline. We aim to respond to each of these publications.

Current IASB documents

Document type	Title	Comment deadline
Exposure Draft*	*Investment Entities–Applying the Consolidation Exception* (Proposed amendments to IFRS 10 and IAS 28)	September 15, 2014
Discussion Paper	*Accounting for Dynamic Risk Management: a Portfolio Revaluation Approach to Macro Hedging*	October 17, 2014

* The AcSB has also published this document for comment to integrate the standard into Part 1 of the *CPA Canada Handbook – Accounting* when the IASB will have published its definitive standard.

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