

# IFRS news

## Will IASB and FASB impairment models be converged?

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**The IASB and FASB impairment models for financial assets could differ if FASB plans to find an alternative to the 'three bucket' approach are successful.**

The IASB and FASB have been deliberating a 'three bucket' impairment model for financial assets. The FASB met recently to discuss the next steps for the project, after announcing its intention to further discuss key aspects of the model. It considered the results of outreach efforts and constituent feedback, and unanimously agreed with concerns from US constituents that aspects of the 'three bucket' impairment model are complex and difficult to understand. The FASB will not therefore move forward with an exposure draft on the 'three bucket' impairment model; it will instead explore a revised approach.

### ***What are the key issues?***

Under the 'three bucket' impairment model, financial assets would initially be placed in 'bucket 1', where impairment losses would only be recognised for those assets expected to experience a loss event in the next 12 months. As credit risk deteriorates, assets would then move to 'bucket 2' or 'bucket 3', where impairment losses would be measured based on lifetime expected losses, irrespective of when the loss event is expected to occur.

Key aspects of the 'three bucket' impairment model include determining whether a loss event is expected to occur in the next 12 months, and the level of credit deterioration that requires a transfer of assets between buckets. Feedback from US constituents indicated defining these concepts may be difficult and raised

concerns over the understandability, operability and auditability of the model. The FASB considered whether implementation guidance could adequately clarify the objectives of the model. It concluded that, even with improved definitions for the key terms, there was still likely to be concern over whether the model results in impairment losses that faithfully represent the credit risk of the portfolio. The FASB therefore directed its staff to explore a model that incorporates the concept of expected losses, but applies that concept to all financial assets held and uses a single measurement approach.

The FASB's decision to explore a revised approach could result in an impairment model that differs from the IASB's model. During that discussion, certain IASB members indicated that they have heard much less concern about the 'three bucket' impairment model; it therefore plans to move forward with that approach.

### ***What is next?***

The FASB directed its staff to develop the new model and is hopeful that the staff will be able to leverage the discussions held to date in that process. Discussions of the new model are expected to take place over the next several weeks, with the FASB sharing its findings with the IASB in September. The IASB has not publicly discussed this FASB decision and whether it will affect its timetable, which is to issue an IASB ED in Q4 2012.

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## ***Five standards to have different effective date in the EU vs rest of world***

**The EU's likely endorsement of a wave of standards for 2014 means that IFRS reporters will have to early-adopt the standards in 2013 if they need to claim compliance with IFRS and EU IFRS.**

The EU is likely to endorse IFRSs 10, 11, 12 and IASs 27 and 28 ('the standards') for financial years starting on or after 1 January 2014, one year later than the mandatory adoption date required by the standards.

The Accounting Regulatory Committee (ARC) voted on 1 June 2012 to recommend endorsement of the standards for adoption in 2014. This recommendation is likely to be accepted by EU; in which case, companies applying IFRS as endorsed by the EU ('EU IFRS') will have to apply these standards, from financial years starting on or after 1 January 2014 at the latest. The EU endorsement is expected to occur by the end of 2012, with early adoption permitted. EU IFRS reporters will be able to early-

adopt the standards in 2013 if they need to claim compliance with IFRS and EU IFRS.

### ***Am I affected?***

All entities that report under EU IFRS will be affected. However, because the application of standards is retrospective, there will not be significant differences carried forward.

### ***What do I need to do?***

EU IFRS reporters should consider the impact of these standards and whether it will be beneficial to early-adopt. Entities that need to comply with both IFRS and EU IFRS may find it beneficial to early-adopt these standards when they are endorsed.

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## ***Cannon Street press***

### ***Leasing re-deliberations end; controversy set to continue***

The IASB and FASB ended their re-deliberations of the leasing project with tentative agreements on a number of issues relating to presentation and disclosure.

However, there is likely to be dissent on a number of areas from some members of

both boards at the proposals in the revised exposure draft.

The revised exposure draft is due to be published late November 2012 and will have a 120-day comment period.

### ***Boards aim to make revenue accounting 'less onerous'***

The IASB and FASB at their July meeting reached tentative decisions on identifying separate performance obligations, performance obligations satisfied over time and onerous performance obligations. They

also discussed the accounting for licences but did not reach any decisions.

Other key issues still to be re-deliberated include the 'reasonably assured' constraint

on recognition of variable consideration, collectibility, time value of money, contract combination and modification, disclosures and transition.

For more information about the latest discussions, [click here](#) to see ‘Straight away: Board re-deliberations to make proposed revenue standard ‘less onerous’ or visit [pwc.com/ifrs](http://pwc.com/ifrs).

### ***SEC releases final report on IFRS ‘work plan’***

The SEC staff has published its final report on its ‘work plan’ intended to help the SEC evaluate the implications of incorporating IFRS into the US financial reporting system. However, the report does not include a decision as to whether IFRS should or should not be incorporated, or how such incorporation should occur. The IFRS Foundation said in response that it ‘regrets’ the report was not accompanied by a recommended action plan.

The report does state that IFRS is generally perceived to be of high quality, although there are areas where gaps remain (for example, accounting for extractive industries, insurance and rate-regulated industries), and inconsistencies in the application of IFRS globally.

It also believes enhancements should be made to the IASB’s co-ordination with individual country standard setters and the IASB’s funding process.

### ***IASB amends transition guidance for IFRSs 10, 11 and 12***

The IASB has issued an amendment to the transition requirements in IFRSs 10, 11 and 12. It clarifies that the date of initial application is the first day of the annual period in which IFRS 10 is adopted – for example, 1 January 2013 for a calendar-year entity that adopts IFRS 10 in 2013. Entities adopting IFRS 10 should assess control at the date of initial application; the treatment of comparative figures depends on this assessment.

A key clarification in the amendment is that adjustments to previous accounting are not required for investees that are consolidated under both IFRS 10 and the previous guidance in IAS 27/SIC 12 as at the date of initial application, or investees that will no longer be consolidated under both sets of guidance as at the date of initial application.

Comparative disclosures will be required for IFRS 12 disclosures in relation to

subsidiaries, associates and joint arrangements. However, this is limited only to the period that immediately precedes the first annual period of IFRS 12 application. Comparative disclosures are not required for interests in unconsolidated structured entities.

The amendment is effective for annual periods beginning on or after 1 January 2013, consistent with IFRS 10, 11 and 12. It will affect all reporting entities (investors) that need to adopt IFRSs 10, 11 or 12.

IFRS preparers should start considering the transition amendment, and how they can use the exemptions granted to minimise implementation costs of IFRSs 10, 11 and 12. IFRS preparers should also start collating the comparative disclosure information required by the amendment.

## **IFRS IC discusses accounting for rate-regulated activities**

The IFRS Interpretations Committee (IC) discussed in its May meeting issues around rate-regulated activities, specifically:

- whether customers within a regulatory jurisdiction can be combined into a single unit of account and if so,
- whether it would be appropriate to recognise assets and liabilities arising out of regulation.

The IC staff recommended that the IASB should add this to its agenda, given that the IASB has listed rate-regulated activities as

a potential project in its Agenda Consultation. However, there was some concern that if the IASB does not address it, the issues will resurface at the IC. So the IC has deferred its decision until it is clear whether the IASB will address the issue.

Entities that are subject to rate regulation might be affected by the ongoing discussions. Management should continue to monitor developments and engage with the IASB and IC on this topic.



## **IFRS quiz: statement of cash flows**

**The preparation of the cash flow statement sounds easy, but it is always the last of the primary statements to be prepared and can give rise to the most questions from users. Test yourself against PwC's statement of cash flows specialist, Tak Yano, with this IFRS quiz. You might also want to read our [topic summary](#) on statement of cash flows to improve your chances of a better score.**

**Q1: What is the principle in IAS 7 for the classification of cash flows?**

- (a) Cash flows should be classified according to the nature of the activity in a manner that is most appropriate to the business; or
- (b) Cash flows in IAS 7 should be classified consistently with the classification of the related item in the statement of financial position.

**Q2: Which criterion is not included in the definition of cash equivalents under IAS 7?**

- (a) Subject to an insignificant change in value;
- (b) Short-term, highly liquid investments;

- (c) Investment in high-quality instruments; or
- (d) Readily convertible to known amounts of cash.

**Q3: Which of the following should be shown as cash and cash equivalents within the consolidated statement of cash flows?**

- (a) A deposit in an escrow account, access to which requires a third party's signature;
- (b) Restricted funds that are not available for use in the short-term and can be used only for specific capital payments; or
- (c) Cash balance held by a subsidiary that cannot be transferred to other parts of the group because of exchange controls.

**Q4: Where can interest paid be classified?**

- (a) Financing activities;
- (b) Operating activities;
- (c) Operating or financing activities; or
- (d) Operating, investing or financing activities.

**Q5: Which of the following expenditures should not be classified as cash flows from investing activities?**

- (a) Payments to acquire property, plant and equipment;
- (b) Payments to acquire intangible assets; or
- (c) Payments for research or exploration.

**Q6: Which of the following statements is false?**

- (a) Cash flows from derivatives held for dealing or trading purposes are classified as operating activities;
- (b) Cash flows from derivatives that are accounted for as hedges under IAS 39 are classified in the same manner as the hedged transactions; or
- (c) Cash flows from commodity derivatives held as 'economic hedges' that do not meet the criteria for hedge accounting in IAS 39 are classified under financing activities.

**Q7: Where is cash acquired in a business combination classified?**

- (a) Operating activities;
- (b) Investing activities; or
- (c) Financing activities.

**Q8: How should the subsequent settlement of deferred consideration for a business combination be classified?**

- (a) As investing activities;
- (b) As financing activities; or
- (c) As either of the above, depending on the facts and circumstances.

**Q9: Entity A acquired an additional 20% interest in a subsidiary. How should management classify the transaction in A's consolidated statement of cash flows?**

- (a) As investing activities;
- (b) As financing activities; or
- (c) There is an accounting policy choice: investing or financing activities.

**Q10: Which of the following is not an acceptable presentation of cash flows from discontinued operations?**

- (a) Nothing in the statement of cash flows and a detailed breakdown of the cash flows from discontinued operations between the three categories is in the notes;
- (b) One line for discontinued operations within each category in the statement of cash flows;
- (c) Each line item analysed between continuing and discontinued operations in the statement of cash flows; or
- (d) Total of cash flows from discontinued operations presented separately from operating, investing and financing activities in the statement of cash flows.

## Answers

**Question 1: A** – The main principle behind the classification of cash flows in IAS 7 is that cash flows should be classified according to the nature of the activity in a manner that is most appropriate to the business of the entity and in accordance with the definitions of operating, investing and financing activities. The IFRS Interpretations Committee noted that it will use this as a guiding principle when analysing future requests on the classification of cash flows.

**Question 2: C** – Cash equivalents are 'short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value'. High-quality instruments might be needed to meet this definition, but they are not a part of the definition.

### Answers (continued)

**Question 3: C** – The definition of cash and cash equivalents in IAS 7 requires the funds to either be on hand or available on demand if cash; or, if a cash equivalent, liquid, readily convertible and subject to insignificant changes in value. The restrictions in fact patterns (a) and (b) are so severe that the balances are unlikely to meet the definition of cash and cash equivalents. The cash in fact pattern (c) is freely available for use within the subsidiary and is included in cash and cash equivalents in the consolidated statement of cash flows. The exchange controls might be disclosed in a note to the statement of cash flows if the matter is deemed significant.

**Question 4: D** – IAS 7 does not mandate the presentation of interest cash flows, but it allows an entity to determine the classification most appropriate to its business. IAS 7 permits interest paid to be classified in operating or financing activities provided the presentation is applied on a consistent basis from period to period. Interest paid is classified as an investing activity when it is capitalised. The IASB has proposed an annual improvement to IAS 7 (in the 2010-2012 cycle) to clarify that interest capitalised should be classified as investing.

**Question 5: C** – Only expenditures that result in a recognised asset in the balance sheet are eligible for classification as cash flows from investing activities under IAS 7. Expenditures such as exploration activities and internal research activities that might be considered by management to be investing for the future but do not result in a recognised asset are not classified as cash flows from investing activities. This is following an amendment to IAS 7 as part of the 2009 annual improvements project.

**Question 6: C** – IAS 7 provides examples of cash flows arising from investing activities, which include cash flows related to derivatives that do not qualify for hedge accounting, are

not held for trading purposes or do not relate to financing activities. Commodity derivatives do not relate to the financing of the business and should not be presented as financing activities.

**Question 7: B** – IAS 7 requires the amounts of cash and cash equivalents paid or received in respect of consideration to be shown under investing activities net of any cash and cash equivalent balances transferred as part of the purchase. It requires disclosure of the amount of cash and cash equivalents in the subsidiary transferred as a result of the acquisition.

**Question 8: C** – Cash subsequently paid for deferred consideration recognised at the acquisition date or any adjustment arising during the measurement period should be classified as investing activities, as these cash flows arise from the recognition of the acquiree's net assets in a business combination. However, if there is clear evidence that the arrangement is in substance a financing transaction (for example, a long-term loan note), settlement of the deferred consideration could be classified as a financing cash flow.

**Question 9: B** – Changes in ownership interests in a subsidiary that do not result in a loss of control, such as the purchase or sale by a parent of a subsidiary's equity instruments, are accounted for as equity transactions under IAS 27. The resulting cash flows are classified in the same way as other transactions with owners, as cash flows from financing activities.

**Question 10: D** – IFRS 5 requires disclosure of the net cash flows attributable to the operating, investing and financing activities of discontinued operations (except for newly-acquired subsidiaries classified as held for sale on acquisition). Disclosing a total of cash flows from discontinued operations on the face of the statement of cash flows does not meet this requirement.





## Russian PIEs move to IFRS in 2012

**Galina Ryltsova, PwC Russia partner and member of the Russian Ministry of Finance's 'Interagency Working Group for IFRS Implementation', looks at recent developments in Russia's adoption of IFRS.**

The use of IFRS is expanding rapidly in Russia and, based on the government's plans, may expand further still. Russian credit institutions, insurance companies and companies whose shares are admitted for trading will need to issue a full set of IFRS consolidated financial statements by 2012. Entities that issue securities through subscription involving a group of over 500 individuals are also required to prepare IFRS consolidated financial statements.

The official date of transition for those companies not already reporting under IFRS is 1 January 2011. IFRS consolidated financial statements need to be audited and filed by 30 April 2013 and published by 31 May 2013 (see box below).

Around 1,000 more companies are expected to be required to prepare IFRS consolidated financial statements in future, although approximately 200 of the largest cos in Russia already prepare IFRS consolidated financial statements.

### *The deadline is looming*

The IFRS transition activity in entities affected by the law has been rather slow to date. Activity levels are expected to rise as the year-end approaches and the deadline of 30 April 2013 moves closer.

The slow start could be a result of lack of detailed descriptions in the new law, a number of cross-references to other federal laws, and lack of clarity over fines and penalties to comply. Fines and penalties also seem low compared to the cost of adopting IFRS. However, consistent with the experience of other countries in adopting IFRS, delays in starting creates challenges in meeting the reporting deadline for all parties. This deadline is just nine months away.

### *Further IFRS developments*

Plans for the further development of accounting and financial reporting in the

### Local background

- **Early 1990s:** Russian companies looking for global capital markets started preparing IFRS financial statements on a voluntary basis.
- **2005:** Mandatory for banks to prepare their financial statements under IFRS.
- **From 2005 to date:** Russia moves towards adopting IFRS, while amending and developing Russian GAAP along IFRS-based lines.
- **From 2011:** The Ministry of Finance requires credit institutions, insurance companies, companies whose shares are admitted for trading and entities placing securities through open or closed subscription involving a group of over 500 individuals to issue IFRS consolidated financial statements by 2012.
- **From 2012:** Those entities not already reporting under IFRS must do so for annual periods beginning on or after January 2011. IFRS consolidated financial statements need to be audited and filed by 30 April 2013 and published by 31 May 2013.
- **From 2015:** Entities that have traded shares or bonds that are already reporting under other internationally recognised rules move to IFRS for consolidated financial statements.

The rules apply to foreign companies' subsidiaries that are listed on the Russian stock exchange as they do to all Russian entities.

Russian Federation based on IFRS have been adopted for 2012-2015, including:

- adoption of IFRS by professional participants on the securities market, incorporated investment funds and their management companies, non-state pension funds, clearing agencies, commodity exchanges, stock exchange brokers and some unitary enterprises, among others;
- preparation of individual financial statements under IFRS;
- a differentiated approach to accounting reporting for different types of entities.

Non-public companies are expected to be able to choose between reporting under Russian GAAP or IFRS following suggestions from the Russian government in April this year for revoking requirements to submit financial statements prepared under Russian GAAP for non-public companies. In addition, the President issued an order in May related to simplifying financial reporting for certain types of economic entities.

### ***Galina's contribution to IFRS adoption in Russia***

IFRS adoption in Russia has taken many years, and a lot of people have been involved in this process. Galina Ryltsova is one of those who played an important role in seeing it through to its current stage. Galina and her team have made a significant contribution to examining and adopting standards as a member of the country's national expert bodies.

Galina has been a member of the National Organisation for Financial Accounting and Reporting Standards (NSFO) since 2003. The NSFO acts as an expert body and works to promote the further development of IFRS in Russia. It includes representatives from all sides: those who prepare and use financial statements, auditors and members of regulatory bodies. The NSFO makes recommendations to regulatory bodies on different aspects of consolidated financial statement reporting, including governing bodies' competence, submission and publication, supervision and other issues relating to practical application.

Galina is also a member of the Interdepartmental Working Group on IFRS Application ('the Group'), set up by The Ministry of Finance in 2012. Its objective is to summarise application practice for the federal law 'On Consolidated Financial Statements' and other regulations on the application of IFRS. As part of implementing

the Group's decisions, the Ministry of Finance can publish the corresponding regulations and instructions, and the Group can publish its views on IFRS application practices.

The Group first met on 3 July 2012. Galina will be tackling the critical issues relating to its future work, including:

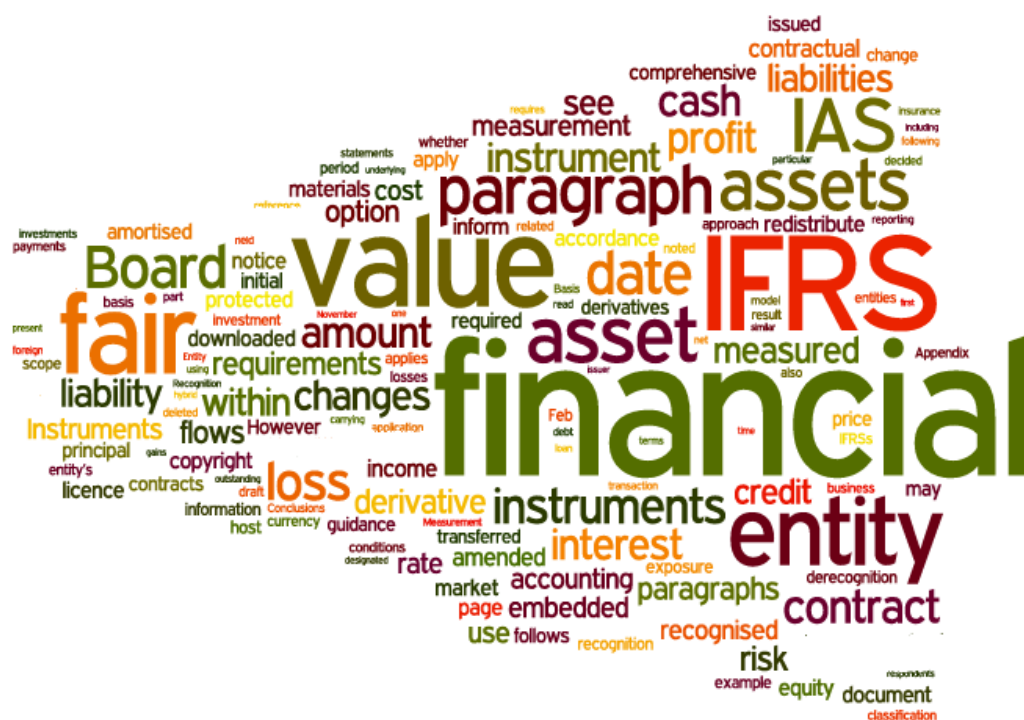
- Standard forms for audit reports issued under the law 'On Consolidated Financial Statements' and references to IFRS vs 'IFRS as adopted in Russia' in audit reports;
- Additional requirements for auditors and audit organisations providing audit services relating to IFRS financial statements prepared under the above law;
- Approval of IFRS consolidated financial statements by the shareholders;
- Auditor approval of IFRS consolidated financial statements;
- Periods of IFRS reporting for newly-listed companies;
- Implications of the early adoption of IFRS that are not yet approved for application in Russia.

These activities allow us to stay one step ahead of the legal developments in the law.



## Guess the IFRS

Word clouds take a given text and present all the words in a pattern that gives greater prominence to words that appear more frequently. What IFRS standard do you think this word cloud represents? (The answer is at the bottom of this page.)



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