IFRS INTERPRETATIONS COMMITTEE - AGENDA REJECTIONS (JULY 2015)

INTERNATIONAL FINANCIAL REPORTING BULLETIN 2015/12

Background

This Bulletin summarises issues that the IFRS Interpretations Committee (the Interpretations Committee) decided not to take onto its agenda at its July 2015 meeting, which were reported in its public newsletter (the IFRIC Update). Although these agenda rejections do not represent authoritative guidance issued by the International Accounting Standards Board (IASB), in practice they are regarded as being highly persuasive. All entities that report in accordance with IFRS need to be aware of these agenda rejections, and may need to modify their accounting approach. More detailed background about agenda rejections is set out below.

The Interpretations Committee is the interpretative body of the IASB. The role of the Interpretations Committee is to provide guidance on financial reporting issues which have been identified and which are not specifically addressed in IFRS, or where unsatisfactory or conflicting interpretations either have developed, or appear likely to develop.

Any party which has an interest in financial reporting is encouraged to submit issues to the Interpretations Committee when it is considered to be important that the issue is addressed by either the Interpretations Committee itself, or by the IASB. When issues are raised, the Interpretations Committee normally consults a range of other parties, including national accounting standard setting bodies, other organisations involved with accounting standard setting, and securities regulators.

At each of its meetings, the Interpretations Committee considers new issues that have been raised, and decides whether they should be added to its agenda. For those issues that are not added to the agenda, a tentative agenda decision is published in the IFRIC Update newsletter which is issued shortly after each of the Interpretations Committee's meetings. These tentative agenda decisions are open to public comment for a period of 60 days, after which point they are taken back to the Interpretations Committee for further consideration in the light of any comment letters which have been received and further analysis carried out by the Staff. The tentative agenda decision is then either confirmed and reported in the next IFRIC Update, or the issue is either subjected to further consideration by the Interpretations Committee's agenda or referred to the IASB.

Interpretations Committee agenda decisions do not represent authoritative guidance. However, they do set out the Interpretations Committee's rationale for not taking an issue onto its agenda (or referring it to the IASB). It is noted on the IFRS Foundation's website that they 'should be seen as helpful, informative and persuasive'. In practice, it is expected that entities reporting in accordance with IFRS will take account of and follow the agenda decisions and this is the approach which is followed by securities regulators worldwide.

STATUS

Final

EFFECTIVE DATE

Immediate

ACCOUNTING IMPACT

Clarification of IFRS requirements.
May lead to changes in practice.

Agenda decisions that were finalised at the July 2015 meeting

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

Tentative agenda decisions at the July 2015 meeting

IAS 2/IAS 38 — *Inventories/Intangible Assets - Should interest be accreted on prepayments in long-term supply contracts?*

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

Each of these is discussed below, split between those which are expected to have wide application and those which are narrower in focus.

Agenda decision at the July 2015 meeting – narrow application

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

The question that was brought to the Interpretations Committee relates to a clarification whether the future minimum funding requirement for contributions to a defined benefit plan to cover future service would apply for only the fixed period that had been agreed between the entity and the pension trustees.

In the fact pattern provided by the submitter, neither a plan wind-up nor a plan closure to future accrual has been decided upon at the end of the reporting period. However, the entity and the trustees were required to renew the schedule of contributions at the end of the fixed period. Accordingly, if the plan continued after the fixed period, the entity would be required to continue to make the enhanced contributions.

IFRIC 14.18 requires an entity to analyse its minimum funding requirements into the contributions that are required to cover:

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

The pension trustees determine some or all of the factors which establish the minimum funding basis. When the entity estimates the future minimum funding requirement contributions it should:

(i) Include the amounts in the schedule of contributions for the fixed period specified by the schedule; and

(ii) Beyond that period make an estimate that assumes a continuation of those factors that establish the minimum funding basis as determined by the pension trustees.

This is due to the requirements in IFRIC 14.21 and BC30 under which the estimate of the future minimum funding requirement contributions does not include the effect of expected changes in the terms and conditions of the minimum funding basis that are not substantively enacted or contractually agreed at the end of the reporting period. The factors which establish the minimum funding basis are equivalent to a legal requirement or contractual agreement.

In addition, it was noted that IFRIC 14.17 and 21 require an entity to use assumptions that are consistent with those used to determine the defined benefit obligation and that exist at the end of the reporting period.

In the light of the existing requirements and the above analysis, the Interpretations Committee decided that sufficient guidance exists, and that it should not add this issue to its agenda.

Tentative agenda decisions at the July 2015 meeting - wide application

IAS 2/IAS 38 Inventories/Intangible Assets – Should interest be accreted on prepayments in long-term supply contracts?

The Interpretations Committee was asked to clarify the accounting for prepayments in a long-term supply contract of raw materials. More specifically the question was raised of whether the purchaser should accrete interest on those long-term prepayments by recognising interest income, resulting in an increase in the cost of inventories and therefore cost of sales.

When payments for an asset are deferred and the arrangement contains a financing element, the difference between the purchase price on normal credit terms and the amount paid is recognised separately as interest expense over the period of financing (IAS 2.18).

This treatment is in line with similar guidance in IAS 16 *Property, Plant and Equipment* and IAS 38 as well as IFRS 15 *Revenue from Contracts with Customers* which further clarifies that a financing component in a transaction is recognised separately for prepayment and deferral of payment.

However, the Interpretations Committee also acknowledged that judgement is required when identifying whether individual arrangements contain a financing component. A prepayment could be in return for something else, such as assurance over the supply of a particular raw material in future.

BDO comment

The tentative decision illustrates that implicit and explicit financing components in the form of prepayments give rise to an interest expenses. This is not only consistent with current IFRSs but also future guidance in IFRS 15 which includes an explicit reference to prepayments and also acknowledges that prepayments or deferred settlement terms do not automatically give rise to a financing component.

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

The submission to the Interpretations Committee is in relation to the accounting for deferred taxes where the tax base of an entity's non-monetary assets and liabilities is not determined in its functional currency, giving rise to deferred taxes due to exchange rate changes. The question is whether these deferred taxes should be recognised in profit or loss.

It was noted that the deferred taxes recognised do not arise from a transaction or event that is recognised outside profit or loss and are therefore recognised in profit or loss in accordance with IAS 12.58. The amounts are not presented with foreign exchange gains or losses but with other deferred taxes in the statement of profit or loss.

The Interpretations Committee noted that it would expect the entity to disclose an explanation in accordance with IAS 12.79 when changes in the exchange rate are a major component of deferred taxes.

BDO comment

The tentative decision clarifies that the treatment of deferred taxes arising from exchange rate changes on the tax basis of non-current assets is based on the underlying transaction which is not recognised in other comprehensive income (OCI) but profit or loss.

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