KPMG
cutting through complexity

# Shaping the future of IFRS

## IASB consults on Conceptual Framework

September 2013, Issue 2013/16

**IN THE HEADLINES**

**kpmg.com/ifrs**

> “Recently there has been much discussion about whether global accounting standards are still fit for purpose. The IASB’s call for input is well-timed to address concerns about IFRS, including the growing complexity in financial reporting.”
>
> – Mark Vaessen
> KPMG’s Global IFRS network leader

## Shaping the future of IFRS

The purpose of the IASB’s Conceptual Framework is to define the core principles to be applied when writing accounting standards. So the Board’s commitment to revise the Conceptual Framework could have a major impact on IFRS in the future. The consultation is at an early stage and the discussion paper (DP) seeks input on a number of topics, including the following key areas:

- how the balance sheet may change;
- how the performance statement(s) may change; and
- how disclosures may change.

Once finalised, the revised Conceptual Framework would hold out the prospect of a set of internally consistent accounting standards, and a faster, less controversial process for producing new standards. The major principles would be settled, not devised afresh each time, and need only be applied to the problem in hand.

This *In the Headlines* highlights the key issues on the table. Whilst they may not affect businesses immediately, they could significantly affect IFRS in the future.

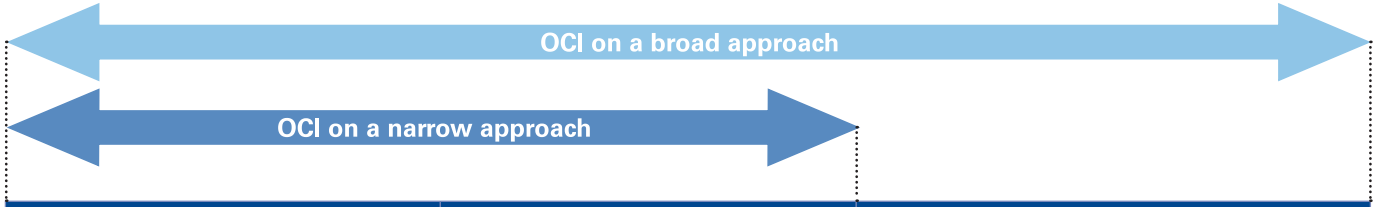
## How the balance sheet may change

| Balance sheet now | How it may change |
|---|---|
| **What is an asset?** | |
| An asset can be a physical object. For example, if an entity leases an aircraft, then it considers the *aircraft itself* in determining whether to record it on the balance sheet. The aircraft *in its entirety* – and not a part of the aircraft – is recorded on or taken off the balance sheet. | An asset could be an individual right in a bundle of rights. Like financial instruments at present, a non-financial asset could be ‘sliced and diced’ from an accounting perspective. An entity would book a *right to use* the aircraft, rather than the aircraft itself – i.e. a ‘slice’ of the aircraft representing the lease thereof, not the whole aircraft. |
| **When is a liability recorded?** | |
| An entity records a liability if it has a present obligation and an outflow (payment) is probable. It does not record a liability if there is significant uncertainty about the existence of an obligation (e.g. an entity is not sure if it has committed a wrongdoing) or about the outcome (e.g. the amount, or whether anything will be paid, is uncertain). An entity generally does not record a liability if it can avoid fulfilling it. | An entity would record a liability regardless of whether it can avoid fulfilling it. All uncertainty about the outcome would be reflected in the measurement. Some uncertain litigation exposures that are currently not recorded unless the uncertainty is reduced would be recognised (or recognised sooner), but at a less certain amount. However, on a standard-by-standard basis the IASB might decide not to require recognition if the uncertainty would be so significant (the threshold is not defined) as to mislead the users. |
| **When can an item be taken off the balance sheet?** | |
| An entity cannot take an asset off the balance sheet if it transfers the asset to another party but is still exposed to the economic risks and benefits related to that asset. For example, if a bank sells some securities to another party but has an obligation to repurchase the securities at a fixed price at a later date and retains substantially all the risks and benefits (a ‘repo’ transaction), then it cannot take these securities off-balance sheet. | An entity would take an asset off balance sheet when it loses control of the legal rights. This could mean that assets may be taken off the balance sheet more easily. For example, repo’d securities could be taken off balance sheet. The IASB acknowledges that it would need to devise rules, on a standard-by-standard basis, for the retained interest – e.g. the obligation to buy back the securities. |
| **How are assets and liabilities measured?** | |
| There is no single measure for assets and liabilities, and there are no set principles for the IASB to require a specific measure. Assets and liabilities are measured at cost, current market prices (including fair value) or another cash-flow-based measurement – e.g. value in use. The use of fair value has been increasing in recent years. | Different measurement bases would be retained. There would be a few principles to help the IASB choose a measure on a standard-by-standard basis – including how an asset contributes to future cash flows and how a liability is settled or fulfilled. It is unclear whether the IASB expects to see a further increase in the use of fair value. |

## How the performance statement(s) may change

The IASB is not considering any radical changes to the performance statements, but increased balance sheet uncertainty in the future could make performance statements more volatile. Instead of defining performance, the IASB is considering which items could be recorded 'below the bottom line' – i.e. in other comprehensive income (OCI) – and which of those should be recycled later 'above the line' – i.e. through profit or loss.

A 'narrow' and a 'broad' approach to profit or loss vs OCI are under consideration. Under the broad approach, all items currently reported in OCI would continue to be recorded there and most, but not all, would be recycled (the IASB would decide on a standard-by-standard basis). Under the narrow approach, some items – e.g. revaluations of assets, remeasurements of pensions and some changes in the fair value of financial instruments under IFRS 9[1] – which are currently booked in OCI would be booked in profit or loss.




| Bridging items | Mismatched remeasurements | 'Transitory' remeasurements |
|---|---|---|
| • Discount rate changes in financial assets (IFRS 9 proposals)<br>• Discount rate changes in insurance contracts (Insurance Contracts 2013 proposals) | • Exchange differences on foreign operations<br>• Cash flow hedges (IFRS 9) | • Revaluations of assets<br>• Remeasurements of pensions<br>• Changes in investments in equity instruments and own credit risk changes in financial liabilities (IFRS 9) |
| **Recycle to P&L** | **Recycle to P&L** | **Recycle some but not all** |

## How disclosures may change

This consultation on the Conceptual Framework is just part of the IASB's disclosure initiative, which comes amid growing calls to cut the clutter from financial reports and make them more relevant to users. The IASB's work on the initiative is summarised below.

| Disclosure initiative | |
|---|---|
| **Conceptual Framework** | **Other possible changes** |
| • Objectives of the primary statements and the notes<br>• Principles guiding the IASB in developing disclosure requirements, and preparers in complying with those | • Guidance on how to apply materiality to disclosures<br>• Narrow-scope amendments to IAS 1[2]<br>• Revision of disclosures in existing standards (or those in development)<br>• Replacement of IAS 1, IAS 7[3] and IAS 8[4] |

"This consultation deals with some fundamental and long-debated issues. It's vital that all stakeholders provide feedback to the IASB on its proposed solutions. This opportunity is not to be missed."

– Mark Vaessen
KPMG's Global IFRS network leader

## Other matters on the table

The DP also covers the following questions.

- Should the discussion about stewardship, reliability and prudence be reopened?
- What is the role of business models in financial reporting?
- What is a 'unit of account'?

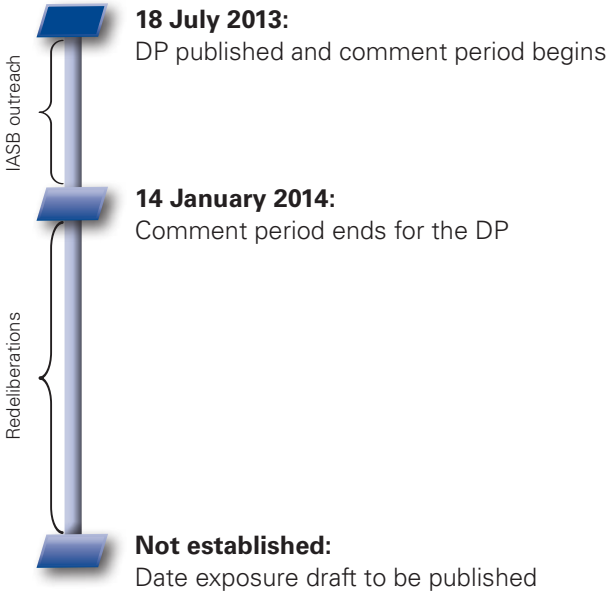
## Next steps

The IASB has requested comments from all interested parties.

The DP is open for comment until 14 January 2014.

For more information on the DP, please go to the *IASB press release* or speak to your usual KPMG contact.

## Timeline




### Endnotes

1 IFRS 9 *Financial Instruments*
2 IAS 1 *Presentation of Financial Statements*
3 IAS 7 *Statement of Cash Flows*
4 IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*



Publication name: *In the Headlines – Shaping the future of IFRS*

Publication number: Issue 2013/16

Publication date: September 2013

KPMG International Standards Group is part of KPMG IFRG Limited.