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IFRS Today

Our series on the most topical issues in IFRS® Standards and financial reporting

11 February 2021

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VIDEO TRANSCRIPT

IFRIC agenda decisions – February's meeting

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Hello – I'm Brian O'Donovan – I'm a partner at KPMG and I'm a member of the IFRS Interpretations Committee – the IFRIC.

In its February meeting, the Committee talked about going concern, we talked about valuation of inventories, and we decided to stop talking about sale and leaseback in a corporate wrapper. Now, remember, if you have a fact pattern similar to one considered by the IFRIC, then you're expected to consider the explanatory material in final IFRIC agenda decisions when preparing IFRS financial statements.

Going concern

Going concern – It's a huge topic, the defining issue of this reporting season. The Committee looked at two very specific aspects of going concern.

Firstly, suppose you're behind with your filings. You're about to authorise multiple sets of financial statements going back several years. Not ideal, but it happens. Very recently, very sadly, you've decided to liquidate the business. You are no longer a going concern. What impact does that have on the financial statements you're about to authorise?

Well, the Committee noted that the decision to liquidate the business, the conclusion that you are no longer a going concern, well it's a post-balance sheet event. Crucially, it's an adjusting event for each of the financial statements you're about to authorise. So none of those – for 2020, 2019, 2018, whatever – none of those financial statements will now be presented on a going concern basis.

The second issue on going concern – well, that was about a different scenario. So now suppose you did file your 2019 financial statements on time on a going concern basis but again you've decided to liquidate the business. What impact does that have when you take your 2019 numbers and include them as comparatives in your 2020 financial statements? Well, the Committee reviewed research prepared by the staff suggesting that in fact there is just no diversity in practice on this question. Companies do not – repeat do not – restate their comparative information if they subsequently cease to be a going concern.

Now, both of these issues will be addressed in a tentative agenda decision in the February IFRIC update. Open for comment for 60 days, that's a comment deadline in mid-April.

Net realisable value – Selling costs

If you sell stuff in your business – whether that's clothes or cars or condominiums, anything you classify as inventory – well, you're probably spending a lot of time thinking about net realisable value at the moment. The Committee discussed what kinds of costs should be deducted in arriving at net realisable value. Specifically, the inventory standard says you should deduct the costs necessary to make the sale. Now, can you limit that deduction just to incremental costs?

Well, to understand this question, you really need to focus on the meaning of 'incremental'. In IFRS Standards, 'incremental' typically refers to a cost that would only be incurred if a specific transaction goes ahead. So, in a selling context – an advertising cost, the salaries of sales staff, even the cost of agency staff if you're paying them by the hour – none of those things are truly incremental in that sense.

So, because that definition is so narrow, because the inventory standard does not use the term incremental in this context, the Committee concluded that in estimating net realisable value, a company cannot – repeat cannot – limit itself to considering just incremental selling costs.

Now again this will be a tentative agenda decision in the IFRIC update – 60-day comment period, ending in mid-April.

Sale and leaseback in a single-asset entity

Suppose you own all the shares in a company. That company owns a single asset – a building – and it has no other assets or liabilities. You sell all of the shares in the company to a third party. You lease back the building. How should you calculate the gain on disposal? Do you book the full gain on deconsolidation of the company? Or do you restrict the gain to reflect the rights you've retained through the leaseback of the building?

In 2020, the Committee published a tentative agenda decision effectively concluding that you would restrict the gain. The question in February was whether or not to finalise that agenda decision. Now, I think most Committee members continued to believe that it's right to restrict the gain in that very narrow fact pattern. But many Committee members thought there were bigger issues here. Suppose you're selling a business, a big complicated business, and you're just leasing back one single asset? Would you still restrict the gain?

Ultimately, the Committee decided not to finalise this agenda decision. Instead, they recommended that the IASB, the Board, look more broadly at the question, hopefully considering bigger, more complicated fact patterns. So no final agenda decision, instead a recommendation that the Board consider narrow-scope standard-setting.

Next steps

The February IFRIC Update will include two tentative agenda decisions – one on going concern, one on valuation of inventories. They will be open for comment with a comment deadline in mid-April. So take a look, see what you think. Think about the impact on your business. Think if you want to take this opportunity to have your say and submit a comment letter.

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Publication name: *IFRIC agenda decisions – February's meeting*

Publication date: February 2021