Special Interest Session

Investor-focused IFRS update

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The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation.

International Financial Reporting Standards

Investor-Focused Update
IFRS Conference
Amsterdam

Who we are:

• IASB:
  – Stephen Cooper, IASB member
  – Patrick Finnegan, IASB member
  – Patricia McConnell, IASB member

• Investor perspectives:
  – Peter Joos, Global Head of Accounting and Valuation Research, Morgan Stanley
  – Dennis Jullens, Lecturer, Valuation and Accounting, Rotterdam School of Management
How will this session work?

• For each topic:
  
  – IASB members will discuss:
    – principal reporting changes effective in 2013,
    – select proposed reporting changes
    – new information available for investors, and
    – effects on financial statements and ratio analysis

How will this session work?

• For each topic:
  
  – Investor representatives will discuss:
    – Benefits of the new information,
    – insights that can be obtained,
    – unresolved issues or questions, and
    – implications for valuation
How will this session work?

• For each topic:
  – Preparer representatives will discuss:
    – Key messages delivered about new standards/disclosures
    – Business implications of new standards/disclosures
    – What are investors asking about new standards/disclosures

Main new requirements effective 2013

• Consolidated Financial Statements – control and new guidance for investment entities (IFRS 10)
• Joint Arrangements -- Proportionate Consolidation – removal of this accounting method (IFRS 11)
• Disclosures
  – for unconsolidated structured entities and disclosures of risks associated with interests in other entities (IFRS 12)
• Employee Benefits—Removal of the corridor method (IAS 19)
• Fair Value Measurement and Offsetting Disclosures
  – fair value disclosures (IFRS 13), and
  – offsetting financial instruments (IFRS 7)
• Presentation – of other comprehensive income (IAS 1) and changes in “own credit” (IFRS 9)
Convergence Projects

- **Revenue recognition**— a more robust framework for the recognition of revenue designed to eliminate inconsistencies across industries and improve disclosures
- **Lease Accounting**— greater transparency about the effects of leasing activities, including: leverage, risks and the assets an entity uses in its operations.
IFRS 10 -- Key Messages

✓ The use of a single consolidation model that applies to all entities (voting and non-voting interest entities) which removes uncertainty about which guidance to apply.

✓ Like the previous guidance, the model is based on determining whether an entity controls an investee.

✓ However, the concept of control is described differently: Control is power, exposure to variable returns, and an investor's ability to use power to affect its amount of variable returns.

IFRS 10 -- Key Messages

✓ Some less-than majority owned entities that were not consolidated, may now be consolidated.

✓ Application guidance added to deal with situations difficult to assess:
  – Agency relationships,
  – Relationships with entities that are designed so that voting rights are not the dominant factor in assessing control, such as structured entities,
  – Potential voting rights and control without a majority of voting rights.

✓ Enhanced Disclosures

✓ Investment companies are not required to consolidate investees that are controlled.
Consolidation Decision Process

Power?

Exposure to variable returns?

Ability to use power to affect its amounts of variable returns?

Consider

Current ability to direct the relevant activities, i.e., the activities that significantly affect the investee’s returns?

Do returns have potential to vary as a result of the investee’s performance?

Is the investor a principal or an agent?

If yes, to all 3

Consolidate

Who and What are affected?

Banks
Insurance companies
Oil and Gas companies
Pharmaceutical companies
Managed Funds

Activities that are affected

Securitisation transactions
Leasing
Unit-linked contracts
Energy contracts
Private equity funds
Financial Statement Effects

**Balance Sheet**
- Assets, liabilities and equity may increase or decrease depending on consolidation decision and previous accounting method.
- Ratios to consider: ROA, Debt/Equity, Book value

**Statement of Profit or Loss and OCI**
- Income, expenses and other comprehensive income may increase or decrease depending on consolidation decision and previous accounting
- Ratios to consider: Interest coverage, Return on sales

**Notes to Financial Statements**
- Information about the investee balance sheet and risks (eg: leases, employee benefit plans, commitments)
- Information related to recurring or non-recurring components of income or expense (eg: significant gains or losses, concentration risks)

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Examples

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Example 1: rights

• An investor acquires 48% of the voting rights of an investee.
• Remaining voting rights held by thousands of shareholders, with less than 1% each

Example 1: Analysis

• Based on the relative size of the other shareholders, investor concludes that a 48% interest would be sufficient to give it control.
Example 2: rights

- Investor A holds 40% of the voting rights of an investee.
- Twelve other investors each hold 5% of the voting right.
- Shareholder agreement: investor A has the right to appoint, remove and set the remuneration of management responsible for directing the relevant activities.
- Two-thirds majority vote of the shareholders is required to change the agreement.

Example 2: Analysis

- Given the ability of Investor A to direct the relevant activities of Investee B through the combination of the shareholders’ agreement and the 40% voting interest, Investor A concludes it controls Investee B, and should consolidate.
- Investor A’s shareholding prevents other parties from changing the contractual relationship it has to direct the relevant activities of Investee B, because such a change requires a two-thirds majority.
Investor Considerations

What are the benefits and insights provided by the new standard/disclosures?

2. Nature of the risks associated with subsidiaries and unconsolidated entities (eg: implicit or explicit commitments to fund subsidiaries or unconsolidated entities)
3. Information about non-controlling interests (significant potential voting rights or puts)
4. Understanding of business strategy: (eg: R&D or production facilities previously unconsolidated, but now consolidated)
5. Identification of earnings and dividend flows (eg: are there tax implications or regulatory restrictions on earnings)
Joint Arrangements

Principal Changes

• Jointly controlled entities as defined in IAS 31 (entities structured through a separate vehicle) will now be accounted for in one of two ways:
  – Some may be treated as joint operations (JOs), which would require the separate recognition of each parties’ assets, liabilities, revenues and expenses.
  – Some may be treated as joint ventures and, thus, are no longer permitted a choice between proportionate consolidation or the equity method. Parties must use the equity method.
Assess the parties’ rights and obligations arising from the arrangement by considering:

(a) the legal form of the separate vehicle
(b) the terms of the contractual arrangement,
and, if relevant,
(c) other facts and circumstances

Parties have rights to the assets and obligations for the liabilities

Joint operation

Parties have rights to the net assets

Joint venture

Accounting for assets, liabilities, revenues and expenses in accordance with the contractual arrangements

Accounting for an investment using the equity method

Who is affected?

### JVs by Industry (1990-2010)

<table>
<thead>
<tr>
<th>Industry</th>
<th>JVs</th>
<th>Relative Relevance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business services</td>
<td>17,610</td>
<td>20.45%</td>
</tr>
<tr>
<td>Software</td>
<td>6,718</td>
<td>7.80%</td>
</tr>
<tr>
<td>Wholesale trade: durable goods</td>
<td>5,840</td>
<td>6.78%</td>
</tr>
<tr>
<td>Investment and commodity firms</td>
<td>4,980</td>
<td>5.78%</td>
</tr>
<tr>
<td>Electronic</td>
<td>3,321</td>
<td>3.86%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>2,545</td>
<td>2.95%</td>
</tr>
<tr>
<td>Wholesale trade: non-durable goods</td>
<td>2,300</td>
<td>2.67%</td>
</tr>
<tr>
<td>Mining</td>
<td>2,297</td>
<td>2.67%</td>
</tr>
<tr>
<td>Oil and gas</td>
<td>2,166</td>
<td>2.51%</td>
</tr>
<tr>
<td>Real estate</td>
<td>1,781</td>
<td>2.07%</td>
</tr>
<tr>
<td>Others</td>
<td>36,577</td>
<td>42.46%</td>
</tr>
<tr>
<td><strong>Total number of JVs</strong></td>
<td><strong>86,135</strong></td>
<td>100.00%</td>
</tr>
</tbody>
</table>

Data source: Thomson Financial SDC Platinum Alliances/Joint Ventures database

(*) A separate vehicle is a separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether these entities have a legal personality.
### Who is affected?

**Country**  
<table>
<thead>
<tr>
<th>Country</th>
<th>% companies with Joint Ventures using proportionate consolidation</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>80.00%</td>
</tr>
<tr>
<td>Germany</td>
<td>33.33%</td>
</tr>
<tr>
<td>Italy</td>
<td>33.33%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>56.25%</td>
</tr>
<tr>
<td>Spain</td>
<td>86.66%</td>
</tr>
<tr>
<td>Sweden</td>
<td>50.00%</td>
</tr>
<tr>
<td>Switzerland</td>
<td>50.00%</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>18.75%</td>
</tr>
</tbody>
</table>


### Who is affected?

**Industry**  
<table>
<thead>
<tr>
<th>Industry</th>
<th>% companies with Joint Ventures using proportionate consolidation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer Markets</td>
<td>46.66%</td>
</tr>
<tr>
<td>Financial Services</td>
<td>48.65%</td>
</tr>
<tr>
<td>Industrial Markets</td>
<td>53.97%</td>
</tr>
<tr>
<td>Information, Communications and Entertainment</td>
<td>47.37%</td>
</tr>
<tr>
<td>Infrastructure and Healthcare</td>
<td>40.00%</td>
</tr>
</tbody>
</table>

Financial Statement Effects

Balance Sheet
• Transition from proportionate consolidation to equity method or transition from equity method to direct recognition will affect gross assets and liabilities.
• Ratios to consider: ROA, Debt/Equity, Book value

Statement of Profit or Loss and OCI
• Transition from proportionate consolidation to equity method or transition from equity method to direct recognition will affect revenues and expenses.
• Ratios to consider: Interest coverage, Return on sales

Notes to Financial Statements
• Information about the investee balance sheet and certain risks (e.g.: leases, employee benefit plans, commitments)
• Information related to recurring or non-recurring components of income or expense (e.g.: significant gains or losses, concentration risks)

International Financial Reporting Standards
Examples

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Example 1: Contractual terms reverse the legal features of the separate vehicle

- Investors A and B (the parties) set up a separate vehicle (entity H) and a Joint Operating Agreement (JOA) to undertake oil and gas exploration, development and production activities.
- The main feature of entity H's legal form is that it causes the separate vehicle to be considered in its own right.

Example 1: continued

- The board of Entity H consists of a director from each investor. Each investor owns 50% of Entity H. Unanimous consent is required for any resolution.
- The JOA specifies that the rights and obligations arising from the exploration, development and production activities shall be shared between the parties (i.e. the permits, the production obtained, all costs associated with the activities, taxes payable etc.) in proportion to each party’s shareholding.
Example 1: Analysis

✓ The parties carry out the JOA through a separate vehicle whose legal form confers separation between the parties and the separate vehicle.

✓ The parties have been able to reverse the initial assessment of rights and obligations arising from the legal form of the separate vehicle in which the arrangement is conducted. This is achieved by agreeing to terms in the JOA that entitle them to rights to assets (permits, production, etc.) and obligations for the liabilities (all costs and obligations arising from the activities) that are held in Entity H.

✓ Therefore, the joint arrangement is a Joint Operation.

Example 2: Other facts and circumstances

• Two parties structure a joint arrangement in an incorporated entity (entity C) in which each party has a 50 per cent ownership interest. The purpose of the arrangement is to manufacture materials required by the parties for their own individual manufacturing processes.

• The legal form of entity C (an incorporated entity) through which the activities are conducted initially indicates that the assets and liabilities held in entity C are the assets and liabilities of entity C.

• The contractual arrangement between the parties does not specify that the parties have rights to the assets or obligations for the liabilities of entity C.
Example 2: continued

- The parties are each obliged to purchase all of the output produced by entity C. Entity C cannot sell any of the output to third parties, unless this is approved by the two parties to the arrangement. Because the purpose of the arrangement is to provide the parties with output they require, such sales to third parties are expected to be uncommon and not material.

- The price of the output is set at a level that is designed to cover the costs of production and administrative expenses incurred by entity C. On the basis of this operating model, the arrangement is intended to operate at a break-even level.

Example 2: Analysis

- The parties carry out the manufacturing through entity C whose legal form confers separation between the parties and the entity.

- Even though neither the legal form nor the contractual arrangement dealing with the manufacturing activity specifies that the parties have rights to the assets, and obligations for the liabilities, other facts and circumstances indicate that the arrangement is a JO.
  - The parties are obliged to purchase all of the output produced
  - The price of the output is set at a level that is designed to cover the costs of production and administrative expenses incurred by entity C.

- Consequently, A and B have rights to substantially all the economic benefits of the assets of the manufacturing arrangement. And, the exclusive dependence of H on the parties to purchase all of its output indicates its liabilities will be settled through the parties’ purchases. Therefore, the joint arrangement is a joint operation.
### Investor Considerations

**What are the benefits and insights provided by the new standard/disclosures?**

1. The shift in accounting methods may influence how future joint arrangements are structured: Issues to consider are: debt arrangements (recourse to non-recourse), borrowing capacity, and covenants.

2. Disclosures providing information about off-balance sheet activities and the implications for the financial flexibility of the reporting entity, particularly information about commitments to contribute funding.

3. Elimination of accounting choices makes the understanding of off-balance sheet activities more comparable and understandable.

4. Performance measures for management compensation may be adjusted because of the effects on reported ratios and pre-tax income.

5. Summarised financial information will be available for each material JV, subject to some aggregation tests. These disclosures are more detailed and more disaggregated compared to those under IAS 31.
IFRS 12 – Disclosure of Interests in Other Entities

Scope

Combined disclosure standard for:

- Subsidiaries
- Joint arrangements
- Associates
- Unconsolidated structured entities
IFRS 12 – Key Messages

- IFRS 12 contains disclosure requirements for an entity’s special relationships with other entities. This will address the issues highlighted by the crisis dealing with the lack of transparency about the risks to which entities were exposed from their involvement with “off-balance sheet” vehicles.
- IFRS 12 also contains disclosure requirements about an entity’s interests in subsidiaries, JVs and associates, and unconsolidated structured entities that provide information about the profit or losses and cash flows available to the investor.

Meeting the disclosure objective

Disclosures

- significant judgements and assumptions made
- information about interests in:
  - subsidiaries
  - joint arrangements and associates
  - unconsolidated structured entities
- any additional information that is necessary to meet the disclosure objective

Strike a balance between overburdening financial statements with excessive detail and obscuring information as a result of too much aggregation
Joint arrangements and associates

Nature, extent and financial effects of interests in joint arrangements and associates, eg

• List and nature of interests in individually-material joint arrangements and associates
• Detailed quantitative summarised financial information for each individually-material JV and associate, and in total for all others
• Fair value of investments in individually material JVs and associates (if published quoted prices available)
• Unrecognised share of losses of JVs and associates
• Nature and extent of any significant restrictions on transferring funds

Nature of, and changes in, the risks associated with the involvement

• Commitments and contingent liabilities
Principal Changes

- Reduction in choices available for the recognition of actuarial gains and losses:
  - **Previously**:
    - Immediate recognition through OCI
    - Immediate recognition through P/L
    - Deferred recognition through P/L (‘corridor approach’)
  - **Now**:
    - Immediate recognition through OCI
- Remeasurements in other comprehensive income
- Use of the net interest approach in reporting changes in defined benefit plans

Who is affected?

- Only companies who do not immediately recognise actuarial gains and losses through OCI

<table>
<thead>
<tr>
<th>Country</th>
<th>Index</th>
<th>Immediate through OCI</th>
<th>Corridor</th>
<th>Immediate through P&amp;L</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>FTSE 100</td>
<td>89%</td>
<td>8%</td>
<td>3%</td>
</tr>
<tr>
<td>Germany</td>
<td>DAX 30</td>
<td>67%</td>
<td>33%</td>
<td>0%</td>
</tr>
<tr>
<td>Germany</td>
<td>Non-DAX 30</td>
<td>25%</td>
<td>64%</td>
<td>11%</td>
</tr>
<tr>
<td>France</td>
<td>CAC 40</td>
<td>55%</td>
<td>45%</td>
<td>0%</td>
</tr>
<tr>
<td>France</td>
<td>Non-CAC 40</td>
<td>46%</td>
<td>48%</td>
<td>5%</td>
</tr>
</tbody>
</table>

Source: Street, D.L. and Glaum, M. (2010), Methods for recognition of actuarial gains and losses under IAS 19, ACCA.
What is the size of the impact?

<table>
<thead>
<tr>
<th>Country</th>
<th>Index</th>
<th>Mean unrecognised actuarial gains and losses (€ mm)</th>
<th>Unrecognised actuarial gains and losses divided by equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>FTSE 100</td>
<td>(2,074.50)</td>
<td>(0.02)</td>
</tr>
<tr>
<td>Germany</td>
<td>DAX 30</td>
<td>(410.45)</td>
<td>(0.02)</td>
</tr>
<tr>
<td>Germany</td>
<td>Non-DAX 30</td>
<td>(4.20)</td>
<td>(0.00)</td>
</tr>
<tr>
<td>France</td>
<td>CAC 40</td>
<td>(242.60)</td>
<td>(0.01)</td>
</tr>
<tr>
<td>France</td>
<td>Non-CAC 40</td>
<td>(53.05)</td>
<td>(0.02)</td>
</tr>
</tbody>
</table>


Financial Statement Effects

**Balance Sheet**
- Equity may decrease (increase) if a company has unrecognised actuarial losses (gains) at transition.
- Comparability enhanced because actual deficit/surplus in DBP will be reported on balance sheet.
- Ratios to consider: ROA, Debt/Equity, Book value

**Statement of Profit or Loss and OCI**
- Net profit may be reduced because it will no longer reflect the expectation of higher returns on assets.
- OCI may fluctuate more because all market related assumptions will be reported here.
- Ratios to consider: Interest coverage, Return on sales

**Notes to Financial Statements**
- Simplifies the reporting of changes in defined benefit plans by introducing the net interest approach
- Information related to average duration of the DBO
- Consider effects on loan covenants or borrowing capacity
Example
Investor Considerations

What are the benefits and insights provided by the new standard/disclosures?

1. Balance sheets will reflect the actual funded status of an entity, which will improve comparability between reporting entities.

2. Statements of comprehensive income will reflect actual economic outcomes – no more smoothing.

3. Perception of financial leverage (and hence financial strength) may affect current or prospective borrowing arrangements.

4. Expansion of disclosure requirements should provide a better understanding of how to evaluate the financial effect of DBP assets and liabilities on the SCI and SFP.

5. Key disclosures to consider: expected contributions in the next reporting period, maturity profile of DBP, sensitivity analysis of DBO, disaggregation of fair value of plan assets.
Convergence Projects

Leases
Questions for investors and analysts

1. Do you believe leases create assets and liabilities?
   - Should they be reported on the balance sheet?

2. Do you agree with the lease presentation on the income statement?

3. When considering the package of information in the main statements, together with the disclosures:
   - What is missing?
   - What is included but not useful for your analyses?

Why a Leases project?

Lessee

- Most lease assets and liabilities are off-balance sheet
- Limited information about operating leases

$1.25 trillion of off-balance sheet operating lease commitments for SEC registrants*

* Estimate according to the 2005 SEC report on off-balance sheet activities
Current adjustments to capitalise leases

**Multiplying current lease expense** *(see graph)*
- Doesn’t take into account differences in lease terms or interest rates

**Discounted projected lease payments**
- Assumptions based on limited information in note disclosures

How the proposals improve financial reporting

<table>
<thead>
<tr>
<th>Existing accounting issues</th>
<th>How the proposals address those issues</th>
<th>How the proposals improve financial reporting</th>
</tr>
</thead>
<tbody>
<tr>
<td>Most lease assets and liabilities are off-balance sheet</td>
<td>Recognition of lease assets and liabilities for all leases of more than 12 months</td>
<td>Greater transparency about lessee’s leverage, assets used in operations and cash flows</td>
</tr>
<tr>
<td>Insufficient information provided about operating leases</td>
<td>Enhanced disclosures</td>
<td></td>
</tr>
</tbody>
</table>
### Lessee accounting model

<table>
<thead>
<tr>
<th>Balance sheet</th>
<th>Income statement</th>
<th>Cash flow statement</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Most equipment/vehicle leases</strong></td>
<td><strong>Most real estate leases</strong></td>
<td><strong>Lessee disclosures</strong></td>
</tr>
<tr>
<td>Right-of-use asset&lt;sup&gt;1&lt;/sup&gt;</td>
<td>Right-of-use asset&lt;sup&gt;1&lt;/sup&gt;</td>
<td>Qualitative</td>
</tr>
<tr>
<td>Lease liability&lt;sup&gt;1&lt;/sup&gt;</td>
<td>Lease liability&lt;sup&gt;1&lt;/sup&gt;</td>
<td>General description of leases</td>
</tr>
<tr>
<td>Amortisation expense</td>
<td>Amortisation expense</td>
<td>Terms of:</td>
</tr>
<tr>
<td>Interest expense</td>
<td>Interest expense</td>
<td>- variable lease payments</td>
</tr>
<tr>
<td>Cash paid for principal and interest</td>
<td></td>
<td>- extension/termination options</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- residual value guarantees</td>
</tr>
</tbody>
</table>

1 Excludes variable lease payments linked to sales or use and most payments in renewal periods—decision taken to reduce cost and complexity.

2 Interest on lease liability available in note disclosures.

### Lessee disclosures

#### Qualitative
- General description of leases
- Terms of:
  - variable lease payments
  - extension/termination options
  - residual value guarantees
- Restrictions and covenants
- Information about leases not yet commenced

#### Quantitative
- Maturity analysis of undiscounted cash flows for each of first 5 years plus total thereafter
- Reconciliation of lease liability
- Expense relating to variable lease payments
- Reconciliation of right-of-use asset by asset class (IASB only)

#### Judgments & Risks
- Nature and extent of risks arising from leases
- Significant assumptions and judgments
The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation.

Examples

Balance sheet impact — Retailer

- **Today no adjustments**
- **Proposals**

No change to Retailer’s income statement or cash flow statement.
Disclosures - Retailer

- Qualitative information about leases, including terms of variable lease payments and extension options
- Quantitative information about amount of variable lease payments linked to sales
- Maturity analysis of undiscounted lease payments for each of first five years and thereafter
- Rollforward of right-of-use asset (IASB only) and lease liability

Balance sheet impact — Airlines 1 and 2

- Total assets
- Debt

Assumptions:
- Fleet of 167 aircraft
- Owned/Leased split (in %)
  - A1: 70/30
  - A2: 30/70
- Discount rate: 8%
Income statement impact — Airlines 1 and 2

Assumptions:
- Discount rate: 8%
- Average lease term:
  - A1: 8 years
  - A2: 11 years
- Aircraft leases in 2nd half of lease term:
  - A1: 90%
  - A2: 75%

Cash flow statement impact — Airlines 1 and 2
Disclosures—Airlines 1 and 2

- Qualitative information about leases
- Maturity analysis of undiscounted lease payments for each of first five years and thereafter
- Roll-forwards of right-of-use asset by asset class (IASB only)
- Roll-forwards of lease liabilities related to aircraft leases and real estate leases

International Financial Reporting Standards

Investor Considerations

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Investor Considerations

**What are the benefits and insights provided by the new proposals?**

1. Assets -- Capitalisation of existing operating leases by lessees will increase asset balances, resulting in lower asset turnover and return on asset ratios compared to operating lease accounting.

2. Liabilities -- For both real estate and equipment leases, reported leverage by lessees will more faithfully reflect economic leverage. At transition, the increase in reported debt will cause working capital ratios to decrease, while debt to equity and other leverage ratios will increase.

3. Income and expense -- The effects on profitability metrics will vary – both at transition and over time.

4. Cash flows -- Capitalisation of operating leases by lessees will cause operating and financing cash flows to change—the change will depend on the nature, classification and size of each lessee’s portfolio and whether the portfolio is increasing or decreasing.

5. Will make companies that primarily lease assets more comparable to companies that purchase assets.

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**Next Steps**

- **Issued Exposure Draft** May 2013
- **Joint Redeliberations** Q413
- **Comment period ends** September 13, 2013
- **New Standard Issued** TBD
- **New Standard Effective** TBD

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Revenue recognition

Core Principle
Recognise revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services.

When?
The company satisfies a performance obligation by transferring a good or service to customer.

How much?
Amount of the transaction price allocated to the transfer of goods or services (ie satisfied performance obligation).
Disclosure requirements

**Objective:** To enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers

Qualitative information about

- Estimates and judgements used
- Performance obligations
- Disaggregation of revenue
- Contract assets and contract liabilities (eg unbilled A/R and deferred revenue)
- Assets recognised from the costs to obtain or fulfill a contract
- Remaining performance obligations (ie Information about long-term contracts)

Transition, effective date and early application

- **Effective date:** annual reporting periods beginning on or after 1 January 2017
- Early application permitted (IFRS)
- **Transition methods**
  - Retrospective transition method (with optional practical expedients); or
  - Alternative transition method (ie cumulative catch-up method)
What are the benefits and insights provided by the new standard/disclosures?

1. Removing inconsistencies and weaknesses in existing revenue recognition standards/practices
2. Providing a more robust framework for analysing revenue – particularly transactions involving multiple elements and delivery of goods or services over time.
3. Simplifying the number of accounting standards an investor must understand across industries and sectors.
4. Improving comparability of revenue across companies and geographies.
5. Establishing a common set of disclosures to permit investors to ask comparative questions and to develop expectations of changes over time.
International Financial Reporting Standards

Fair Value Measurement
Offsetting Disclosures
Presentation Changes

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation

Fair Value Measurement -- Principal Changes

- Single set of requirements for all fair value measurements
- Use of a three level 'fair value hierarchy'
  - Level 1: inputs are quoted prices in active markets for identical assets or liabilities that the entity can access
  - Level 2: inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
  - Level 3 unobservable inputs for the asset or liability
- Increased disclosure:
  - for valuation techniques and inputs used to measure fair value
  - on the uncertainty inherent in fair value measurements
Fair Value Measurement - Disclosure

- Information about an entity’s valuation processes is required for fair value measurements categorised within Level 3 of the fair value hierarchy.
- A narrative discussion is required about the sensitivity of a fair value measurement categorised within Level 3.
- Quantitative sensitivity analysis is required for financial instruments measured at fair value.

Disclosure Example

Illustrative Example 15 - Fair values at the end of the reporting period and level of the fair value hierarchy for recurring fair value measurements…

<table>
<thead>
<tr>
<th>Description</th>
<th>31/12/X9</th>
<th></th>
<th></th>
<th>Total gains (losses)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Quoted prices in active markets for identical assets (Level 1)</td>
<td>Significant other observable inputs (Level 2)</td>
<td>Significant unobservable inputs (Level 3)</td>
<td></td>
</tr>
<tr>
<td>Recurring fair value measurements</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trading equity securities&lt;sup&gt;a&lt;/sup&gt;</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real estate industry</td>
<td>93</td>
<td>70</td>
<td>23</td>
<td></td>
</tr>
<tr>
<td>Oil and gas industry</td>
<td>45</td>
<td>45</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>35</td>
<td>15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total trading equity securities</td>
<td>173</td>
<td>130</td>
<td>23</td>
<td></td>
</tr>
<tr>
<td>Other equity securities&lt;sup&gt;a&lt;/sup&gt;</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial services industry</td>
<td>150</td>
<td>150</td>
<td></td>
<td>53</td>
</tr>
<tr>
<td>Healthcare industry</td>
<td>163</td>
<td>110</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy industry</td>
<td>32</td>
<td>32</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private equity fund investments&lt;sup&gt;b&lt;/sup&gt;</td>
<td>25</td>
<td>25</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>15</td>
<td>15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total other equity securities</td>
<td>407</td>
<td>275</td>
<td>110</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Disclosure Example — continued

Illustrative Example 15 - Fair values at the end of the reporting period and level of the fair value hierarchy for non-recurring fair value measurements...

<table>
<thead>
<tr>
<th>Non-recurring fair value measurements</th>
<th>26</th>
<th>26</th>
<th>(15)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets held for sale(c)</td>
<td>26</td>
<td>26</td>
<td>(15)</td>
</tr>
<tr>
<td>Total non-recurring fair value measures</td>
<td>26</td>
<td>26</td>
<td>(15)</td>
</tr>
</tbody>
</table>

\(a\) On the basis of its analysis of the nature, characteristics and risks of the securities, the entity has determined that presenting them by industry is appropriate.

\(b\) On the basis of its analysis of the nature, characteristics and risks of the investments, the entity has determined that presenting them as a single class is appropriate.

\(c\) In accordance with IFRS 5, assets held for sale with a carrying amount of C$35 million were written down to their fair value of C$26 million, less costs to sell of C$6 million (or C$20 million), resulting in a loss of C$15 million, which was included in profit or loss for the period.

(Note: A similar table would be presented for liabilities unless another format is deemed more appropriate by the entity.)

More information about Level 3

- Quantitative disclosure of unobservable inputs and assumptions used
- Description of valuation process in place
- Sensitivity analysis:
  - narrative discussion about sensitivity to changes in unobservable inputs, including inter-relationships between inputs that magnify or mitigate the effect on the measurement
  - quantitative sensitivity analysis for financial instruments
More information about Level 3 continued

Illustrative Example 17 – Quantitative information about significant unobservable inputs used

<table>
<thead>
<tr>
<th>Description</th>
<th>Fair value at 31/12/X9</th>
<th>Valuation technique(s)</th>
<th>Unobservable input</th>
<th>Range (weighted average)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other equity securities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Healthcare industry</td>
<td>53</td>
<td>Discounted cash flow</td>
<td>weighted average cost of capital</td>
<td>7% - 9% (8.1%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>long-term revenue growth rate</td>
<td>2% - 4% (3.2%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>long-term pre-tax operating margin</td>
<td>3% - 6% (4.5%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>discount for lack of marketability</td>
<td>5% - 10% (7.5%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>control premium</td>
<td>1% - 5% (3%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Valued comparable companies</td>
<td>EBITDA multiple(a)</td>
<td>10 - 13 (11.5)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>revenue multiple(b)</td>
<td>1.5 - 2.0 (1.7)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>discount for lack of marketability</td>
<td>5% - 20% (17%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>control premium</td>
<td>1% - 5% (3%)</td>
</tr>
<tr>
<td>Energy industry</td>
<td>32</td>
<td>Discounted cash flow</td>
<td>weighted average cost of capital</td>
<td>6% - 9% (7.2%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>long-term revenue growth rate</td>
<td>3% - 5.5% (4.2%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>long-term pre-tax operating margin</td>
<td>7.5% - 13% (9.2%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>discount for lack of marketability</td>
<td>5% - 10% (7.5%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>control premium</td>
<td>1% - 5% (3%)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Valued comparable companies</td>
<td>EBITDA multiple(a)</td>
<td>6.5 - 12 (9.5)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>revenue multiple(b)</td>
<td>1.0 - 3.0 (2.0)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>discount for lack of marketability</td>
<td>5% - 10% (7.5%)</td>
</tr>
<tr>
<td>Private equity fund investments</td>
<td>25</td>
<td>net asset value(c)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

An entity might disclose the following:

- for the group within the entity that decides the entity’s valuation policies and procedures:
  - its description;
  - to whom that group reports; and
  - the internal reporting procedures in place (eg whether and, if so, how pricing, risk management or audit committees discuss and assess the fair value measurements);
- the frequency and methods for calibration, back testing and other testing procedures of pricing models;
- the process for analysing changes in fair value measurements from period to period;
- how the entity determined that third-party information, such as broker quotes or pricing services, used in the fair value measurement was developed in accordance with the IFRS; and
- the methods used to develop and substantiate the unobservable inputs used in a fair value measurement.
Illustrative Example 19 – Narrative discussion about sensitivity to changes in unobservable inputs

An entity might disclose the following about its residential mortgage-backed securities to comply with this disclosure requirement:

The significant unobservable inputs used in the fair value measurement of the entity’s residential mortgage-backed securities are prepayment rates, probability of default and loss severity in the event of default. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement. Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

Offsetting -- Principal Changes

IFRS 7

• Maintained current offsetting model for financial assets and liabilities – a company has a legally enforceable right to set off the recognised amounts – and added additional application guidance.
• New disclosure requirements for financial assets and liabilities that are:
  – Offset in the statement of financial position; or
  – Subject to master netting arrangements or similar agreements
• Disclosures will be provided by type of financial instrument:
  – Amounts subject to netting arrangements but not set off in the balance sheet will be presented by type of financial instrument or counterparty
Offsetting Example 1

Assumptions
Company A owes CU1,000 to Company B. Company B owes CU800 to Company A. They have a legally enforceable agreement stating that they can offset amounts that are due to each other in all circumstances. They will settle the amounts owed by Company A paying Company B CU200.

Analysis
Company A and Company B would be required to present net amounts in their statements of financial position because they have an unconditional right of set-off and they will settle the amounts net.

Offsetting Example 2

Assumptions
Company A has a derivative asset of CU9,000 with Company B. Company A also has a derivative liability of (CU10,000) with Company B. The companies have entered into a master netting agreement. Under the terms selected, they are allowed to offset amounts due only if one of the companies defaults or goes into bankruptcy. There is no offset allowed in any other circumstances.

Analysis
Company A and Company B would be required to show gross amounts in their statement of financial position because they do not have an unconditional right of set-off.
### IFRS 7– Offsetting Disclosures

**Financial assets subject to offsetting, enforceable master netting arrangements and similar agreements**

<table>
<thead>
<tr>
<th>Description</th>
<th>(a)</th>
<th>(b)</th>
<th>(c) - (a) - (b)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross amounts of recognised financial assets</td>
<td>200</td>
<td>80</td>
<td>120</td>
</tr>
<tr>
<td>Gross amounts of recognised financial liabilities set off in the statement of financial position</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net amounts of financial assets presented in the statement of financial position</td>
<td>90</td>
<td>90</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>290</td>
<td>80</td>
<td>210</td>
</tr>
</tbody>
</table>

### IFRS 7– Offsetting Disclosures

**Net financial assets subject to enforceable master netting arrangements and similar agreements, by counterparty**

<table>
<thead>
<tr>
<th>Related amounts not set off in the statement of financial position</th>
<th>(c)</th>
<th>(d)</th>
<th>(e) = (c) - (d)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net amounts of financial assets presented in the statement of financial position</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial instruments</td>
<td>20</td>
<td>80</td>
<td>10</td>
</tr>
<tr>
<td>Cash collateral received</td>
<td>90</td>
<td>90</td>
<td></td>
</tr>
<tr>
<td>Net amount</td>
<td>210</td>
<td>170</td>
<td>30</td>
</tr>
</tbody>
</table>

Counterparty A 20  -  (10)  10
Counterparty B 100 (80) (20) -
Counterparty C 90  (90)  -  -
Other          -  -  -  -
Total          210 (170) (30) 10
IFRS 7 Disclosures: Benefits for investors

- Provide transparency about significant differences that arise between the net amounts presented in accordance with IFRSs and those presented in accordance with US GAAP, particularly for entities that have large amounts of derivative activities, and will result in increased comparability between the amounts presented in accordance with both sets of standards.
- Provide information to understand the amounts that have been set off in an entity’s balance sheet.
- Provide investors with better information to assess an entity’s credit and cash flow risks that result from the entity’s rights of set-off and related arrangements.

Other Presentation Changes

IFRS 1

- The statement of profit or loss and OCI must be presented in two sections, profit or loss and other comprehensive income.
- Entities will continue to have the choice to present items of profit or loss in a separate statement of profit or loss.
- Entities will be required to group items presented in OCI on the basis of whether they would be reclassified to (recycled through) profit or loss at a later date.

IFRS 9

- The effects of changes in own credit are presented in OCI if a non-derivative financial liability is measured at fair value.