Conceptual Framework Feedback session

Tom Scott, IASB Board Member
Anne McGeachin, Technical Principal

World Standard-setters Conference 2018

#IFRS_WSS

Background

- On 1 October 2018 the participants of the WSS conference discussed examples included in Agenda Paper 5A of the meeting.
- The participants were asked to:
  - apply the concepts in the *Conceptual Framework* to examples in two areas: cryptocurrencies and variable and contingent consideration; and
  - ignore any requirements in IFRS Standards that could apply to those examples.
- The examples aimed to demonstrate how the concepts could guide the Board in developing accounting requirements, not to predict the future outcome of any research or standard-setting activities in these areas.
- These slides summarise the views expressed by the participants of the WSS conference on the examples.

Example 1.1 – Holding cryptocurrencies for investment purposes

- Predominant view: both cryptocurrencies **meet the definition** of an asset
  - ➢ Most agreed that there is a right that is controlled as a result of a past event
  - ➢ Both Crypto and NewCoin have a potential to produce economic benefits (the inflow does not have to be probable or likely)
- Predominant view: holdings in both coins **should be recognised**
  - ➢ Most would recognise NewCoin even though there is significant measurement uncertainty associated with it. Some would recognise it at zero
  - ➢ One of factors driving recognition was that non-recognition would lead to recognition of a day 1 loss which would not faithfully represent the transaction
  - ➢ Non-recognition suggested only if:
    - the market is illiquid which means very high measurement uncertainty and
    - there is no contract entitling entity to exchange cryptocurrency for cash, goods or services

Example 1.1 – Holding cryptocurrencies for investment purposes (continued)

- Predominant view on measurement: **fair value** would provide most useful information
  - ➢ Driven by:
    - characteristics (variability)
    - contribution to cash flows (cash flows through sale only)
  - ➢ Minority view: historical cost – a price at year end would not provide relevant information due to extreme price volatility
  - ➢ Few suggested measurement at zero if there have been no transactions for a long time and it is not expected that the cryptocurrency will recover in the future
  - ➢ If there is no active market, determining fair value may be very difficult especially if a cryptocurrency can produce cash flows only through sale
- Majority supported the use of **P&L** for remeasurements
- **Disclosures** should focus on nature of cryptoassets, reasons for holding them and associated risks
  - ➢ Those who selected historical cost suggested that fair value should be disclosed
- The same conclusions if the company trades in cryptocurrencies

Example 1.2 – Holding cryptocurrency as a medium of exchange

- Predominant view: TradeUCoins **meet the definition** of an asset and **should be recognised**
- **Measurement**:
  - ➢ Many suggested that fair value would provide most useful information
  - ➢ Some suggested measurement could depend on whether the prices are set in the cryptocurrency:
    - - If so, historical cost could be more relevant

Example 1.3 – 'Mining' cryptocurrency

- Predominant view: 'mined' cryptocurrency **meets the definition** of an asset should be **recognised**
- **Measurement**:
  - ➢ Some thought that the selection of measurement should not depend on how the asset is acquired
  - ➢ Predominant view on ***initial measurement***: fair value of received coins
    - Little support for measurement at cost of inputs (perhaps only if the was a correlation between the costs incurred and the value of coins received)
    - Measurement at cost of inputs would not recognise revenue until sale
    - If historical cost basis is selected, fair value of received coins can be used as a deemed cost at initial recognition
  - ➢ ***Subsequent measurement*** could depend on how the cryptocurrency will be used
  - ➢ Many supported subsequent measurement at fair value
- Majority supported the use of **P&L** for remeasurements
- **Disclosures:** information about the differences between the costs of mining and the value of coins received, success rate in mining

Example 1.4 – Initial coin offerings

7

- Predominant view: crypto tokens **meet the definition** of an asset even if it is a right to access something that does not yet exist
- Predominant view: holdings of mined cryptocurrency **should be recognised**
  - Fall in value may suggest that there is an expectation that the e-platform will not be completed
  - But not if the secondary market is very small and most acquirers intend to use tokens, not sell them
- **Measurement**:
  - Some supported fair value based on characteristics of the token
  - Some suggested historical cost because the tokens are likely to contribute to cash flows indirectly by being used to acquire services on e-platform
  - Some suggested dual measurement – fair value more relevant for the statement of financial position, historical cost for financial performance
- Majority supported the use of **P&L** for remeasurements
  - Some support for use of OCI if dual measurement model is selected
- **Disclosures:** information about the likely success or failure of the e-platform to which the value of the tokens is linked

IFRS

Observations on cryptocurrency examples

8

- Some questioned the nature of cryptocurrencies:
  - What is their economic nature? Are they a 'gambling instrument'? Or are they similar in nature to some commodities?
  - Misleading to call it a 'currency' if it does not convey the same rights as a currency backed by a government
- Many advised against standard-setting for cryptocurrencies, so as not to appear to legitimise these activities
- Some considered the effect of possible restrictions on the use of cryptocurrencies:
  - Most thought cryptocurrency held would still be an asset if the holder retained the rights and it was possible that the regulation would change
  - A few doubted that a right existed, or that it is controlled, if holding cryptocurrencies is illegal
- Stronger case for recognition if cryptocurrencies can be used for different purposes
- The purpose for holding cryptocurrencies is important, especially for measurement
- Examples suggested that different accounting models may be necessary for different transactions in cryptocurrencies

IFRS

Example 2.1 – Contingent consideration payable if a milestone is reached

- Predominant view: the company acquires a **single right** when it acquires a patent
  - ➢ Splitting rights was not considered helpful unless they can produce separate cash flows
- Different views on whether acquisition of the patent leads to a single obligation:
  - ➢ Some thought there is a ***single obligation*** arising when the asset is transferred (however some doubt regarding no present ability to avoid additional payment)
  - ➢ Some suggested that the obligation to pay contingent consideration is a ***separate obligation***
- If the obligation to pay contingent consideration is viewed as a separate obligation, many do not see it as a liability at the acquisition date:
  - ➢ The company may have ***present ability to avoid*** transfer
    - Intent to develop and register is not sufficient
    - Contractual terms may be important (eg contractual obligation to submit documents for recognition)
  - ➢ Some questioned what would be the ***past event*** in this case:
    - The *Conceptual Framework* suggests an earlier event than granting of the approval, but not necessarily the acquisition of the right

Example 2.1 – Contingent consideration payable if a milestone is reached (continued)

- Outcome uncertainty, measurement uncertainty and cost constraint were identified as factors to consider in **recognition**
- **Measurement** if only one liability:
  - ➢ Predominant view that the measurement should include an estimate of contingent consideration (on an expected value basis)
  - ➢ Few suggested that the measurement should be equal to the value of additional payment (ie the probability of outcome should not be considered)
- Different views on presentation of **remeasurement** of the lia**bility**:
  - ➢ Users may find it more intuitive to see the changes reflected in the value of the asset
    - however, there is no basis for it if the asset is accounted at cost
  - ➢ Some suggested different development costs are added to the cost of the asset, revaluations may be part of these costs
  - ➢ Many would present the remeasurements of the liability in P&L, even if some effects could be counter-intuitive (eg a failure of the drug could result in a gain in P&L)
- **Disclosures** about significant estimates and judgements made

Example 2.2 – Contingent consideration that depends on the number of users

- Most saw no difference to example 2.1 and reached similar conclusions
- One right / one obligation view was marginally more popular for this example:
  - There is no 3rd party is involved, so the outcome largely depends on the company
  - But some thought there was no liability for the additional payment at least until the programme was broadcast
- Measurement uncertainty is more likely to be a factor in this case: estimating future viewing figures is very uncertain

General observations

- The participants found the case studies a useful illustration of how the *Conceptual Framework* would be used in standard setting
- Many expressed an opinion that the *Conceptual Framework:*
  - helps structure the thought process
  - sets the right factors to consider
- Many found that the *Conceptual Framework* is helpful in reaching decisions:
  - but some issues may be more challenging than others, eg the use of OCI and determination of past event

Join the IFRS Foundation team

visit go.ifrs.org/careers

IFRS

Get involved

Find out more: www.ifrs.org

Follow us:

@IFRSFoundation

IFRS Foundation
International Accounting Standards Board

IFRS Foundation

IFRS Foundation

Join our team: go.ifrs.org/careers

IFRS