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HKFRS / IFRS UPDATE 2012/10

PROPOSED IMPROVEMENTS TO IFRSs 2011 – 2013 CYCLE

HKICPA is seeking comments on the IASB Exposure Draft of *Annual Improvements to IFRSs 2011-2013 Cycle*. The proposed effective date for the amendments is for annual periods beginning on or after 1 January 2014. When these proposals are finalised, it is expected that HKICPA would adopt the amendments to HKFRS following its policy of converging HKFRS with IFRS.

HKICPA's comment period will be closed on 16 January 2013. Alternatively, you may submit your comments to the IASB by 18 February 2013.

STATUS
Exposure Draft

EFFECTIVE DATE
To be confirmed but expected to be for annual periods beginning 1 January 2014 with earlier application permitted

ACCOUNTING IMPACT
May be significant

Background

On 20 November 2012 the International Accounting Standards Board (IASB) published Exposure Draft *ED/2012/2 Annual Improvements to IFRSs 2011 – 2013 Cycle* which sets out proposed amendments to four IFRSs under the annual improvements project. The IASB has adopted the annual improvements process to deal with non-urgent but necessary amendments to IFRSs.

The proposed amendments address the following IFRSs:

- IFRS 1 *First-time Adoption of International Financial Reporting Standards*
- IFRS 3 *Business Combinations*
- IFRS 13 *Fair Value Measurement*
- IAS 40 *Investment Property*

The proposed effective date for the amendments, if finalised, is for annual periods beginning on or after 1 January 2014. It is proposed that earlier application is permitted for all of the amendments.

Proposed amendments

IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Issue: Meaning of effective IFRSs

The improvement clarifies the meaning of 'each IFRS effective at the end of an entity's first IFRS reporting period' as used in IFRS 1.7. The issue addressed by the improvement is which version of an IFRS should be applied by an IFRS first time adopter in circumstances where a new or a revised IFRS that is not yet mandatory, but that can be adopted early, has been issued.

The IASB proposes to amend the basis of conclusions to state that an entity has an option to use either the currently mandatory IFRS or the new IFRS that is not yet mandatory, if that new IFRS permits early application.

A first time adopter that chooses to early apply a new IFRS that is not yet mandatory but that permits early application will be required to apply that new IFRS in all periods presented in its first IFRS financial statements, unless that new IFRS provides an exemption or an exception that permits or requires otherwise.

IFRS 3 *Business Combinations*

Issue: Scope exceptions for joint ventures

IFRS 3 currently includes a scope exemption for the formation of a 'joint venture'. This term had a general meaning under IAS 31 *Interests in Joint Ventures* and covered jointly controlled entities, jointly controlled operations and jointly controlled assets. The issue arises as the wording for the scope exemption was not amended when IAS 31 was replaced by IFRS 11 *Joint Arrangements* which uses the term "joint venture" to describe a specific arrangement. Under IFRS 11 all joint arrangements are classified into either 'joint ventures' or 'joint operations'. This means that not all 'joint arrangements' are covered by the scope exemption in IFRS 3.

There was also uncertainty over whether the exemption applied only to the accounting by the joint arrangement in its own financial statements or to the accounting by the parties to the joint arrangement for their interest in the joint arrangement.

The proposed amendments to IFRS 3 clarify that:

- The formation of all types of joint arrangements as defined in IFRS 11 (ie joint ventures and joint operations) are excluded from the scope of IFRS 3
- The scope exception only applies to the accounting by the joint arrangement in its own financial statements and not to the accounting by the parties to the joint arrangement for their interests in the joint arrangement.

IFRS 13 *Fair Value Measurement*

Issue: Portfolio exception - Scope of paragraph 52

IFRS 13.52 defines the scope of the exception that permits an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis. This is referred to as the portfolio exception.

Under current IFRS 13 it is not clear whether the portfolio exception includes all contracts that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments* if this has been adopted early) even if they do not meet the definition of financial assets and financial liabilities in IAS *32 Financial Instruments: Presentation* (eg some contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments).

The proposed amendment to IFRS 13.52 clarifies that the portfolio exception applies to all contracts within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments* if this has been adopted early), regardless of whether they meet the definition of financial assets or financial liabilities in IAS 32 *Financial Instruments: Presentation.*

IAS 40 *Investment Property*

Issue: Clarifying the interrelationship of IFRS 3 *Business Combinations* and IAS 40 *Investment Property* when classifying the acquisition of investment property as an asset acquisition or as a business combination

It was noted that there is divergence in practice in delineating the scope of IFRS 3 *Business Combinations* and IAS 40 *Investment Property*. Some viewed IFRS 3 and IAS 40 as mutually exclusive when considering the accounting required for the acquisition of an investment property with associated insignificant ancillary services and that such an acquisition is of a single asset called 'investment property'. Others did not view those two standards as being mutually exclusive or the definitions of a business in IFRS 3 and of an investment property in IAS 40 as being interrelated.

The IASB noted that:

- IAS 40.7-15 provides guidance on whether or not property is owner-occupied property or investment property.
- IFRS 3 Appendix A defines the term 'business'.
- Neither IFRS 3 nor IAS 40 contains a limitation of scope that applies when the other standard applies and they are not mutually exclusive
- Judgement is required to determine whether or not a transaction is the acquisition of an investment property or the acquisition of a group of assets or a business combination in the scope of IFRS 3 that includes an investment property.

The amendment to IAS 40 clarifies that:

- Judgement is required to determine whether the acquisition of investment property is the acquisition of an asset, a group of assets or a business combination in the scope of IFRS 3
- The judgement of whether it is a business combination is based on the guidance in IFRS 3 and not on IAS 40.7–15
- The judgement needed to distinguish investment property from owner-occupied property is based on IAS 40.7–15 and not the judgement of whether or not a transaction is a business combination.

BDO's support and assistance on HKFRS/IFRS

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