



Beyond the GAAP

Mazars' newsletter on accounting standards

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Editorial

At the end of June, Hans Hoogervorst, Chair of the International Accounting Standards Board, has stepped down after a 10-year tenure. Andreas Barckow, who has previously served on several IFRS Foundation advisory bodies, has taken over for a first mandate as head of the IASB as of 1 July.

Over the past 10 years, the IASB has published several important standards: IFRS 15 on revenue recognition and IFRS 9 on financial instruments in 2014, IFRS 16 on leases in 2016 and IFRS 17 on insurance contracts in 2017. Though this last standard is not yet effective, it has already been modified and it is expected to be further amended to facilitate the transition as presented in this issue.

As the IASB changes its chairman and several Board members are replaced, the IASB's work plan is still ambitious, with major projects to be completed, such as the one on primary financial statements. As shown by the decisions made in June, maintenance of existing standards is also a priority for the Board which notably intends to propose limited amendments to IAS 7 – *Statement of Cash Flows* and IFRS 7 – *Financial Instruments: Disclosures* in order to improve the information disclosed in the context of reverse factoring arrangements.

IFRS Highlights

Primary Financial Statements project: IASB reaches decision on management performance measures

Following the first redeliberations on the Primary Financial Statements project in March 2021 (see Beyond the GAAP no. 153, March 2021), the International Accounting Standards Board (IASB) has, as expected, gone on to discuss potentially expanding the scope of its requirements for management performance measures (MPMs). The 2019 exposure draft specified that certain minimum disclosures on MPMs would be required, to be presented in a single note to the financial statements.

The IASB decided in March that it would explore possible approaches to expanding the scope of MPMs, beyond what was specified in the exposure draft. The exposure draft defined MPMs as including only certain subtotals of income and

expenses in the statement of profit or loss, namely those that:

- are used in public communications outside financial statements;
- complement totals or subtotals “specified” by IFRS standards (in particular in accordance with the future *General Presentation and Disclosures* standard); and
- communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.

Primarily in order to avoid having to put a new exposure draft out for comment, which would significantly delay the project, the IASB tentatively decided to stick with its original proposals, but to include the numerator or denominator of a ratio in the scope of its requirements for MPMs, if that numerator or denominator meets the definition of an MPM.

This would thus include subtotals of income and expenses that are used solely for a ratio, such as adjusted EBITDA used solely in an adjusted EBITDA/net debt ratio. The IASB hopes that this will increase transparency and discipline in disclosures on MPMs.

The IASB has also tentatively decided not to expand the scope of MPMs to include the following:

- measures based on line items presented in the statement of profit or loss;
- measures based on the cash flow statement;
- measures based on the statement of financial position; and
- ratios.

In practice, this means that widely used measures such as free cash flow and net debt will continue to be excluded from the IASB's definition of MPMs. However, they will still be covered by guidelines from regulators such as ESMA on alternative performance measures (APMs).

IASB work plan: maintenance projects added

Following the IASB meeting on 22 and 23 June, the IASB has updated its work plan (available [here](#)).

The main changes relate to the addition of some narrow-scope projects. There have also been some minor changes to project timetables. The key points of the changes are presented below.

Maintenance projects:

- Initial Application of IFRS 17 – *Insurance Contracts* and IFRS 9 – *Financial Instruments* (exposure draft scheduled for July 2021): addition of a narrow-scope amendment to IFRS 17 on

comparative information (see next article);

- Supplier Finance Arrangements (exposure draft scheduled for the fourth quarter of 2021): addition of narrow-scope amendments to IAS 7 – *Statement of Cash Flows* and IFRS 7 – *Financial Instruments: Disclosures* (see the article in this newsletter);
- Classification of Debt with Covenants as Current or Non-current (exposure draft scheduled for the fourth quarter of 2021): addition of a limited-scope amendment to IAS 1 – *Presentation of Financial Statements* (see the article in this newsletter);
- Lease Liability in a Sale and Leaseback: project direction to be decided in the fourth quarter of 2021 (rather than the third quarter, as previously).

Research projects:

- Dynamic Risk Management: project direction to be decided in the first half of 2022;
- Pension Benefits that Depend on Asset Returns: a review of the initial research is now scheduled for the fourth quarter of 2021 (rather than the third quarter, as previously).

Proposed narrow-scope amendment to IFRS 17 – *Insurance Contracts* on applying a classification overlay

Following preliminary discussions in May, the IASB decided in June to propose a narrow-scope amendment to IFRS 17 in order to facilitate initial application of IFRS 17 – *Insurance Contracts* and IFRS 9 – *Financial Instruments* by insurance entities.

The problem had been discussed previously, during the amendments to IFRS 17 project in 2018. As things stand, the transition

provisions for initial application of IFRS 9 stipulate that the presentation of comparative information in accordance with the new standard is optional. If an entity decides to apply IFRS 9 to comparative information, it may only do this for financial instruments that still exist at the transition date. In other words, financial assets that have been sold or that have matured prior to the transition date shall still be accounted for in accordance with IAS 39 – *Financial Instruments: Recognition and Measurement*, while those that still exist shall be restated in accordance with IFRS 9.

This rule, which was initially intended to smooth transition to IFRS 9, is proving difficult to apply, as it requires entities to distinguish between financial assets and this cannot be done ahead of time. It also creates accounting mismatches with the associated insurance liabilities (particularly for assets measured at amortised cost or at fair value through profit or loss in accordance with IAS 39). Entities may also elect not to account for their assets in accordance with IFRS 9 in the comparative information, whereas comparative information on insurance liabilities must be restated in accordance with IFRS 17.

The IASB's proposed solution (still tentative at this stage) is to amend IFRS 17 to permit the use of a "classification overlay" for initial application of IFRS 17, allowing each financial instrument that is "related to insurance contract liabilities" to be classified in the comparative information as if IFRS 9 had been applied to it (even though some of these financial instruments no longer exist at the transition date). This "classification" approach would not involve applying all the accounting provisions of IFRS 9; some of the rules, such as those on expected credit losses, would not apply.

The proposed amendment is to be published in July, with a shorter comment period of two months. This accelerated process will permit insurance companies to benefit from the amendment when preparing the comparative information for 2022, in time for initial application of IFRS 17 (and IFRS 9) at 1 January 2023.

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Supplier Finance Arrangements: proposed narrow-scope amendments to IAS 7 – *Statement of Cash Flows* and IFRS 7 – *Financial Instruments: Disclosures*

Following the work begun by the IFRS Interpretations Committee (see Beyond the GAAP no. 150, December 2020), the IASB decided at its June meeting to propose an amendment to IAS 7 – *Statement of Cash Flows* in order to meet the information needs of investors regarding supplier finance arrangements, such as reverse factoring or similar arrangements.

The proposed amendment is expected to include new disclosure requirements:

- the key terms and conditions of the supplier finance arrangement;
- the following information, at the start and end of the reporting period:
 - i. the aggregate amount of payables that are part of such arrangements;
 - ii. among the aggregate amount of the payables disclosed under (i), those for which suppliers have already received payment from the finance provider;
 - iii. the range of payment terms, expressed in time, of payables disclosed under (i); and
 - iv. the range of payment terms, expressed in time, of trade payables that do not form part of the arrangement.

The IASB is also proposing to add supplier finance arrangements as an example of information to disclose on liquidity risk in accordance with IFRS 7 – *Financial Instruments: Disclosures*, to help readers of financial statements to better understand the risks related to such arrangements.

The IASB will decide on the transition arrangements for the proposed amendment

at a future meeting. The exposure draft is scheduled for publication in the fourth quarter of 2021.

Classification of Debt with Covenants as Current or Non-current: proposed narrow-scope amendment to IAS 1 – *Presentation of Financial Statements*

In December 2020, the IFRS Interpretations Committee published a tentative agenda decision to clarify, through worked examples, the practical application of the January 2020 amendments to IAS 1 – *Presentation of Financial Statements* (see Beyond the GAAP no. 140, January 2020) on the classification of debt as current or non-current.

In the light of comments received on the agenda decision, the IASB is now proposing to amend IAS 1 again to make the following clarifications on the “specified conditions” (that is, the debt covenants with which the entity must comply):

- if the right to defer settlement for at least 12 months after the end of the reporting period is subject to an entity complying with specified conditions *after* the reporting period, then failure to meet those conditions at the reporting date would not affect the classification as current or non-current for these liabilities;
- however, the entity must disclose information on the following in the notes:
 - i. the conditions (for example, the nature of and date by which the entity must comply with the condition);
 - ii. whether the entity is in compliance with the conditions at the reporting date; and
 - iii. whether and how the entity expects to comply with the conditions by the date on which they are contractually required to be tested.

The IASB is also proposing that non-current liabilities subject to conditions in the next 12 months should be presented in a separate line of the statement of financial position.

Finally, the IASB is proposing to specify that an entity does not have a right to defer settlement at the reporting date when the liability could become repayable within 12 months:

- at the discretion of the counterparty or a third party (for example, when a loan is callable by the lender at any time without cause); or
- if an uncertain future event occurs (or does not occur) and the event's occurrence (or non-occurrence) is unaffected by the entity's future actions (for example, default by a debtor when the entity has provided a guarantee against such default).

In light of these new developments, the IASB is planning to defer the effective date of the amendments to IAS 1 until 1 January 2024 at the earliest, whereas they were originally scheduled for 1 January 2023. An exposure draft of the proposed amendments is scheduled for publication in the fourth quarter of 2021.

IASB Chair Hans Hoogervorst steps down at end of June

At the IFRS Foundation Conference on 3 June 2021, Hans Hoogervorst delivered his farewell speech, available [here](#). It provided an opportunity for him to review the key events and changes of his ten-year term, and to hand over the reins to Andreas Barckow.

IFRS IC agenda decision on Costs Necessary to Sell Inventories (IAS 2 – Inventories)

In June 2021, the IFRS Interpretations Committee (IFRS IC) published an agenda decision on the costs that an entity includes as 'estimated costs necessary to make the sale' when determining the net realisable value of inventories.

The question was whether an entity should include all costs necessary to make the sale or only those that are incremental to the sale.

Based on the definition of net realisable value in paragraph 2 of IAS 2 – *Inventories*, and further drawing on paragraphs 28 to 33 which specify how an entity should estimate the net realisable value of inventories, the IFRS IC concluded that IAS 2 does not permit an entity to limit these costs to incremental costs only.

The Committee stated that only including incremental costs, and excluding those that an entity must incur to sell its inventories but that are not incremental to a particular sale, could fail to achieve the objective set out in paragraph 28 of IAS 2, namely that inventories should be written down where necessary to their net realisable value.

IFRS IC agenda decision on going concern (IAS 10 – *Events after the Reporting Period*)

In June 2021, the IFRS IC published a final agenda decision on two questions relating to going concern issues if an entity is no longer a going concern in period N:

- can it prepare financial statements for prior periods on a going concern basis (given that it was a going concern in those periods) if it has not previously prepared financial statements for those periods?; and
- must it restate comparative information that was previously published on a going concern basis to reflect the new situation?

In response to the first question, the Committee stated that IFRS 10.14 and IAS 1.25 do not permit an entity to prepare financial statements on a going concern basis once it is no longer a going concern.

In response to the second, the Committee noted that standard practice is not to restate comparative information, and thus there is not sufficient diversity in practice to warrant a standard-setting project. We can thus conclude that it is acceptable not to restate previously-published comparative information, and that in such a situation, only period N must be presented so as to reflect the fact that the entity is no longer a going concern.

European Highlights

EFRAG launches consultation on both the IASB's future agenda and its own research programme

Readers will remember that the IASB is currently consulting on its work plan for the next five years (see Beyond the GAAP no. 154, April 2021). The comment period is

open until 27 September 2021. In the hope of benefiting from potential synergies, EFRAG has launched a consultation (available [here](#)) that covers both the IASB's future agenda and its own research programme.

EFRAG is proposing that the IASB's priorities should be as follows:

1. Connecting financial and sustainability reporting, starting with climate-related financial information;
2. Crypto-currencies and related transactions;
3. Discontinued operations and disposal groups;
4. Intangible assets;
5. The statement of cash flows and related issues; and
6. Variable and contingent considerations.

Responses should be sent to EFRAG by 16 September 2021, either in the form of a comment letter or by replying to the online survey.

EFRAG publishes its annual review for 2020

On 3 June 2021, EFRAG published its annual review for 2020 (available [here](#)). It reminded readers of its key mission: to serve the European public interest in the field of corporate reporting. EFRAG also emphasised its increasing involvement in sustainability reporting over the period, in line with the European Union's shift towards a sustainable economy. This has resulted in EFRAG taking on responsibility, in 2021, for preparatory work on future sustainability reporting standards.

EFRAG launches consultation on due process for future European sustainability reporting standards

As part of the project to revise the European Non-Financial Reporting Directive and replace it with the Corporate Sustainability Reporting Directive (CSRD) (see Beyond the GAAP no. 154, April 2021), EFRAG has been put in charge of developing non-financial reporting standards, and must provide technical advice to the European Commission to support the adoption of European Sustainability Reporting Standards (ESRS).

As with accounting standards, the development of sustainability standards must follow a clear and rigorous due process, ensuring that EFRAG's work to develop its technical advice is carried out with an appropriate level of transparency.

EFRAG's proposed due process procedures, on which it has just launched a public consultation (available [here](#)), are based on the recommendations in the report from EFRAG President Jean-Paul Gauzès on the need for changes to the governance and funding of EFRAG, which was published on 8 March 2021 (see Beyond the GAAP no. 153, March 2021).

Readers will remember that the CSRD proposal specifies that the European Commission will adopt the first set of sustainability reporting standards by 31 October 2022.

EFRAG's public consultation is open until 15 September 2021.

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