

IAASB CAG PAPER



International Federation of Accountants

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Agenda Item

H

Committee: IAASB Consultative Advisory Group

Meeting Location: London

Meeting Date: September 14-15, 2010

IAASB – IASB Liaison

Objectives of Agenda Item

1. To provide an update on key IAASB – IASB liaison activities.
2. To provide an update on new IAASB Working Groups to be established by the IAASB to monitor selected IASB projects for verifiability/auditability issues.¹

Papers to be Referred to during Discussion

3. The discussion on this topic will follow the structure of this CAG Paper.

Matters for CAG Consideration

A. Update on Key IAASB – IASB Liaison Activities

IASB Expert Advisory Panel on Impairment of Financial Assets

4. Since February 2010, the IAASB has been observing meetings of the IASB Expert Advisory Panel (EAP) on impairment of financial assets at the invitation of the IASB. The objectives of the EAP are two-folds:
 - (a) To make recommendations to the IASB and US Financial Accounting Standards Board (FASB) on how operational challenges of the IASB's Expected Cash Flow approach and that of the FASB's might be resolved; and
 - (b) To assist in organizing and running field testing of any proposals made by the IASB.
5. The formation of this EAP follows the IASB's exposure draft on *Financial Instruments: Amortized Cost and Impairment* and is in response to the 2008 recommendations by the Financial Stability Forum. Represented by its Chairman, and for meetings he could not attend, the Deputy Chair or Technical Director, the IAASB has observed physical and teleconference meetings of the EAP during February 2010 – June 2010.²

¹ More information on the Working Groups is provided later in this CAG paper (see section B).

² The EAP meets every four-six weeks up to June 2010.

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6. In itself, the IASB's invitation to the IAASB to observe its EAP meetings signals a step forward in fostering closer working relationship between the two Boards. Furthermore, observing these meetings also enables the IAASB to better achieve its objective of providing timely input to the IASB during early stages of its deliberations.
7. Importantly, participation in the EAP has provided better insight into the approaches preparers may take to comply with the IASB's proposals. The auditability of the approaches and the reliability (that is, sources of evidence) of the inputs on which to base the estimates of impairment were frequently discussed in the EAP meetings. The final recommendations made by the EAP to the IASB, although not specifically identified as points on "auditability", would address some of the more difficult aspects of the ED proposals to manage from a preparer's perspective, including being able to verify the amounts recorded. In general, these discussions provided reassurance that the IASB's proposals, particularly once the EAP comments have been taken into account, do not necessarily pose the auditability concerns that were initially feared. Plans are underway for a joint meeting of members of the IAASB and the IASB. The IASB has identified the auditability of their current proposals as one of the three topics on which they would like to seek input during the meeting.

Submission to Exposure Draft on IFRS Taxonomy

8. A response to the International Accounting Standards Committee Foundation (IASCF) on its exposure draft *International Financial Reporting Standards (IFRS) Taxonomy 2010* was submitted in April 2010. Whilst not commenting on the technical specifications within the taxonomy itself, the response drew attention to the IAASB's XBRL project and the Staff Questions and Answers publication issued in January 2010. Support was also expressed for the continued development and enhancement of taxonomies for IFRS and IFRS for SMEs following due process and broad consultation.

Progress of IAASB Working Groups

Liabilities

9. The Liabilities Working Group submitted a response in May 2010 to the IASB on its exposure draft *Measurement of Liabilities in IAS 37 Provisions, Contingent Liabilities and Contingent Assets* (**see Agenda Item H.1**). The response highlighted a number of verifiability/auditability challenges that may arise as a result of the IASB's proposals and provided recommendations on how they may be addressed. In doing so, the Working Group encouraged the IASB to consider the importance of the guidance providing adequate explanation of the intent of the requirements and encouraged the IAASB to include relevant explanations in non-authoritative staff documents in the final standard. The Working Group noted this is an important basis for ensuring consistency in interpretation by both preparers and auditors. The IASB is currently considering responses to the exposure draft. It intends to issue the final IFRS in Q1/Q2 2011.

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Fair Value Measurement

10. Representatives of the Fair Values Working Group held a teleconference in May 2010 with IASB staff responsible for the Fair Value Measurement project. IASB Staff provided updates on key IASB decisions made in this regard thereby allowing the Working Group to assess how comments raised in its response to the IASB exposure drafts³ had been addressed. The majority of the points made by the Working Group in its written response had been addressed by the IASB.
11. A limited re-exposure draft relating to measurement uncertainty analysis for fair value measurements was issued on 29 June, with responses due 7 September. In addition, the IASB may develop further guidance of an educational nature in 2011 to address the more challenging areas of the project.

Conceptual Framework—The Reporting Entity

12. The Conceptual Framework Working Group discussed the IASB's exposure draft *Conceptual Framework for Financial Reporting: The Reporting Entity* and came to the view that there are no significant verifiability/auditability issues for raising with the IASB. The conclusions of the Working Group (that it does not perceive that there are auditing challenges arising from the IASB's proposals) were communicated to the IASB during a liaison meeting held in July 2010. The comment period ended on July 16, 2010.

Monitoring Developments on Disclosures

13. During the IAASB's annual review of financial reporting trends in December 2009, the IAASB recognized the increasing importance of financial statement disclosures which has raised questions about how auditors approach them in their audits and the judgments involved in relation to disclosures when assessing the fair presentation of financial statements. Issues related to disclosures have linkages to a number of existing IAASB projects for example, the projects to revise ISA 720⁴ and IAPS 1012.⁵ During a similar discussion at the March 2010 CAG meeting, Representatives expressed support for the IAASB's attention on this topic.
14. Subject to respondents' comments on its *Strategy and Work Program, 2012-2014*, the IAASB envisaged it will undertake a project on auditing financial statement

³ Exposure Draft ED/2009/5, *Fair Value Measurement*, Exposure Draft ED/2009/7, *Financial Instruments: Classification and Measurement*, and IASB Discussion Paper DP 2009/2 *Credit Risk in Liability Measurement* and Request for Information ('Expected Loss Model') *Impairment of Financial Assets: Expected Cash Flow Approach*.

⁴ ISA 720, *The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements*

⁵ IAPS 1012, *Auditing Derivative Financial Instruments*

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disclosures.⁶ In many liaison meetings with stakeholders, it has become clear to the IAASB that the issues related to disclosures transcend both financial reporting and auditing, and that stakeholders have differing perspectives and expectations. Active liaison with the IASB is, therefore, particularly important in this context.

15. In this regard, IAASB leadership has also been taking the opportunity to discuss the challenges of the increasing role and importance of disclosures in various meetings with, for example, the Financial Stability Board and regulators (in particular, financial institutions regulators). As a result of such discussions, IAASB Deputy Chair has been appointed as an observer to the Advisory Panel of the European Financial Reporting Advisory Group for their project on the development of a disclosures framework.

16. In connection with the IASB's current work plan, the following key projects are relevant:

- *Management Commentary Project.* The project's objective is to develop a best practice model for a narrative report that would accompany but be presented outside of the financial statements, setting out management's explanation of the entity's financial condition, changes in financial condition, results of operations, and causes of changes in material line items. This project plays a complementary role to the other IASB project on Conceptual Framework (see below).⁷

Although non-binding, the proposals arising from this project will have implications for the audit of financial statements (and therefore disclosures) if reporting entities elect to apply the proposed IASB model. In particular, the interplay between information disclosed in the notes to the financial statements and disclosures presented outside of the financial statements (i.e., the boundaries of disclosures) may have implications for the auditor's procedures for obtaining sufficient audit evidence, and the auditor's responsibilities for other information in documents containing financial statements that may be closely related to the financial statements (for example, ISA 720).

- *Conceptual Framework Project.* Phase E (Presentation and Disclosure including Financial Reporting Boundaries) of the IASB's Conceptual Framework project aims to determine the concepts underlying presentation and disclosure of financial information. This phase is currently inactive and a timeline has yet to be communicated by the IASB.

Of particular relevance is the work that is anticipated to be undertaken to determine the boundaries of information for achieving the objective of general purpose financial reporting. As the applicable financial reporting framework forms the basis

⁶ The IAASB has established a Working Group tasked to bring forward for the IAASB's consideration, recommendations regarding the scope, direction and proposal for a new project on Disclosures.

⁷ The IASB has indicated it intends that Phase E (Presentation and Disclosure) of the Conceptual Framework project will build upon its work in the Management Commentary project.

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for the auditor's opinion, the nature and extent of disclosures required by the IASB's framework will have a direct influence on the procedures the auditor has to perform so as to be satisfied with management's assertions regarding the presentation and disclosure of classes of transactions, accounting balances, and disclosures.

- *Disclosures in Subject Matter Specific Projects.* Several IASB's projects include proposals for new disclosures. For example, the fair value measurement project aims to introduce enhanced disclosures regarding fair value measurements, including proposed disclosures regarding sensitivity analyses and the correlation of inputs.⁸ The IASB's discussion paper on *Extractive Industries* also proposes new disclosures on reserves. These are some examples of areas that need to be monitored by the IAASB.

17. The IAASB is slated to further discuss the topic of auditing financial statement disclosures at its September 2010 meeting, with a proposal to develop an issues paper that would set out the issues related to disclosures from an auditing perspective. Updates in this regard will be provided at CAG meetings in 2011.

B. New IAASB Working Groups

18. At its June 2010 meeting, the IAASB discussed anticipated key activities in the IASB's forward work program with the aim of identifying projects that the IAASB should monitor for auditability/verifiability issues. The IAASB agreed that for those projects where IAASB working groups are currently in place,⁹ these working groups will continue to monitor their respective IASB projects.
19. Informed by responses to the questionnaire issued in April 2010 to inform the development of its *Strategy and Work Program, 2012-2014*,¹⁰ the IAASB further identified other projects for monitoring. The IASB is anticipated to undertake consultation activities for these projects during the remainder of 2010. A summary of anticipated activities of the IASB and status of the respective IAASB working groups is provided in the appendix to this paper.

⁸ These proposals are expected to be exposed by the IASB for public comment soon.

⁹ Fair Value Measurement & Financial Instrument, Revenue Recognition, Leases, Income Taxes, Emissions Trading Scheme, and Conceptual Framework. Each IAASB working group is led by a rapporteur and consists of at least two IAASB members, and may include technical advisors or, where relevant, official IAASB observers. IAASB participants indicate their interest in participating in working groups to the IAASB Liaison Representatives or IAASB Staff.

¹⁰ In April 2010, the IAASB issued a questionnaire to inform the development of its strategy and related work program for the period 2012-2014. The comment period closed on May 14, 2010. Amongst other matters, respondents were asked to identify financial reporting projects, in addition to those currently monitored by the IAASB, which may inform the IAASB's future agenda.

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20. In addition, a joint meeting of representatives of the IAASB and the IASB is being planned for early autumn to discuss a number of specific proposals the IASB is considering and on which they would like early reaction from an auditability perspective. This is a further step forward in fostering closer working relationship between the two Boards and another way for the IAASB to provide input early in the IASB's development process.

Matters for CAG Consideration

1. Representatives are asked to note the update and raise any other matters which may be of relevance.

Material Presented – IAASB CAG PAPER

Agenda Item H.1

IAASB's Submission to the IASB's Exposure Draft *Measurement of Liabilities in IAS 37 Provisions, Contingent Liabilities and Contingent Assets*

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APPENDIX

Forward IASB Work Program and Status of IAASB Working Groups¹¹

Active Projects	Working Group Status	Publication - Comments Due Date ¹²
Extractive Activities	New	Discussion Paper - Jul 30 ¹³
Revenue from Contracts with Customers	Not yet active	Exposure Draft - Oct 22
Financial Statement Presentation (Items of other comprehensive income)	New	Exposure Draft - Sept 30
Fair Value Measurement (Measurement uncertainty analysis disclosure)	Active	Exposure Draft - Sept 7
Insurance Contracts	New	Exposure Draft – Nov 30
Activity Anticipated	Working Group Status	Publication - Release Date
Financial Instruments (Hedge accounting)	Active (See Fair Value Measurement)	Exposure Draft - Q3
Leases	Active	Exposure Draft - Q2
Income Taxes	In Place	Exposure Draft - Q3/Q4
Emissions Trading Scheme	In Place	Exposure Draft - Q4
Conceptual Framework (Phase C: Measurement)	Active	Discussion paper - Q4

¹¹ The IAASB does not anticipate that comments will be submitted for the following:

- Exposure Draft on Conceptual Framework: Reporting Entity (Comments due July 15, 2010)
- Exposure Draft on Financial Instruments: Fair Value Option for Financial Liabilities (Comments due July 16, 2010)
- Exposure Draft on Defined Benefit Plans (Comments due September 6, 2010)

¹² Underlined publications are hyper-linked to the respective documents on the IASB's website.

¹³ Comments will not be submitted by the IAASB to the IASB's Discussion Paper but the IASB's discussion and next steps in the project will continue to be monitored.