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IASB® *Investor Update*

Our newsletter for the investment community

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The IASB's Investor Update *highlights market-relevant accounting topics that could impact the companies that investors follow. It also shares with investors information on the IASB's standard-setting activities and insights from our ongoing dialogue with the investment community. We invite investors seeking further detail on accounting proposals and current requirements to contact us.*

www.ifrs.org/Investor-resources

Editors' welcome

Welcome to the first issue of the International Accounting Standards Board's (IASB) *Investor Update*—a newsletter that aims to make it easy for investors to keep up to speed on changes in the world of International Financial Reporting Standards (IFRS) and how those changes may affect an investor's day job.

You may wonder why an accounting standard-setter is writing a newsletter for investors, or indeed why investors should be interested in the work we are doing.

While we concede that technical accounting can be a dry topic (although we have had some surprisingly emotive discussions!), financial information remains the lifeblood of all fundamental investment decisions. The IASB writes accounting standards to ensure that this financial information is as useful as possible to investors in making decisions, but we cannot do that in isolation—we need your help.

However, we find that investors are often wary of speaking to us. Some don't think it's their job. Others are afraid that they will find themselves drawn into detailed technical accounting discussions. Still others aren't interested in the accounting requirements until they are finalised: don't call me until it affects me!.

The *Investor Update* aims to break through these barriers. Each issue will profile the impact that recently introduced Standards may have on your analysis of performance. We will highlight changes that are in the pipeline and signal how they might alter the way in which you look at companies. And we flag when and how you can best share your thoughts on the direction we are taking.

We hope that you will find the *Investor Update* useful and that it encourages you to engage with us. However, as with everything we do, we would appreciate your candid feedback on how we might continue to improve in the future.

We look forward to hearing from you.

In this issue:

- We need your views
- Spotlight on disclosures
- Insights on the changes to revenue recognition
- IASB in profile
- Events calendar

We need your views

The IASB sets Standards for you, the investor. But we can't do this in isolation. We need your help in understanding whether potential changes to the Standards will provide you with the information that you analyse and that ultimately drives your investment decisions.

You do not have to be an accountant to speak to us. It is the insight that you offer as one who uses financial information to make investment decisions that is important to us.

The following are the current topics/projects on which we are seeking your views. Some apply to all companies while others are industry-specific.

The *Conceptual Framework for Financial Reporting*

What is it? The *Conceptual Framework* sets out the concepts that the IASB uses to set Standards.

What are we doing? This project includes:

(a) obtaining a better understanding of how investors use (or don't use) the information in 'other comprehensive income' so we can develop guidance for what could be reported in other comprehensive income instead of in profit or loss;

(b) understanding whether investors receive the right information about the different types of claims on an entity so we can decide whether to classify those claims as liabilities or equity; and

(c) understanding investors' views on prudence and stewardship.

Click here to read Steve Cooper's Investor Perspective on this project.

Rate-regulated activities

What is this project about? In many countries governments regulate pricing and supply in key industries. The industries often include gas, water or electricity supply. We refer to this as 'rate regulation'.

Why are we doing a project? Rate regulation can have a significant impact on the timing and amount of a company's revenue, and on the certainty of related cash flows. However, IFRS does not provide any specific accounting guidance for these companies. We would like to understand if there is a need for specific accounting for these types of activities.

Dynamic risk management

What is it? For companies with revenues and profits that are exposed to market price movements, risk management activities can be quite complex, often involving the risk management of portfolios of exposures that continuously change. We often refer to this as dynamic risk management or macro hedging.

Why are we doing a project? It is challenging to reflect this form of risk management in companies' financial statements with the current accounting requirements. We have published a Discussion Paper to explore how to better reflect companies' dynamic risk management activities in their financial statements.

Click here to read Steve Cooper's Investor Perspective on this project.

Disclosures

What are we doing? We are considering focused amendments to improve the notes to the primary financial statements (what we are referring to as 'disclosures' in this newsletter). Among these are:

(a) high level changes to clarify current requirements, including removing perceived barriers to providing investors with more relevant information; and

(b) providing better information about the non-cash movements in debt (for example, foreign exchange effects or debt acquired in a business combination).

See our Spotlight on Disclosures section for more information on this project.

Accounting for business combinations

What are we doing? We are reviewing IFRS 3 *Business Combinations* to determine whether it is working as expected, including whether it results in useful information for investors.

We are asking, for example, whether the accounting for intangible assets versus goodwill and the related impairment provides useful information to investors; and whether the current accounting for assets acquired and liabilities assumed is helpful.

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Spotlight on disclosures

Time and again we hear from investors that the 'primary' financial statements on their own are not enough. In the absence of good quality notes to these financial statements the investor is 'flying blind'.

As the IASB looks to improve financial reporting, it actively seeks input from investors and other stakeholders on areas where they would like to see changes to disclosures.

What have we heard?

In general, while companies and investors agree that financial reports are an important communication tool, they tell us that turning the required data into useful information can often be a challenge.

For example:

Connecting the dots—management may not think that they can apply judgement when deciding how to order information in the notes to the financial statements. As a result, information on the same topic (for example, debt or derivatives) may be spread across different notes, making it hard for investors to find and connect relevant information.

Seeing the bigger picture—investors tell us that it can be difficult to spot the areas that warrant extra attention in the midst of often very lengthy notes. Contributing to this issue are the different interpretations of materiality by management. Because the cost of failing to disclose an item that is subsequently deemed material is high, management is often hesitant to exclude items from the notes.

Compliance vs communication—a number of disclosures are boilerplate, containing little 'signal' for investors.

Making sense of the numbers—investors have suggested a number of areas in which existing notes could be improved:

(a) more information is needed for investors to understand the non-cash movements (for example, foreign exchange effects or debt acquired in a business combination) in debt;

(b) better information about the maturity of debt is needed, as well as clearer disclosures of any restrictions on the repatriation of cash;

(c) better disclosure is needed about the total consideration paid for an acquisition (for example, debt acquired, pension liabilities assumed).; and

(d) better descriptions of the intangibles acquired in a business combination are needed.

What is the IASB doing about this?

The IASB hosted a Discussion Forum on disclosures in January 2013. The dialogue helped us better understand investor views about this area of financial reporting. As a result:

(a) we obtained a clearer picture of the 'disclosure problem'. We are exploring ways of addressing some of the problems highlighted.

(b) we published a Feedback Statement summarising what we heard and potential next steps for the IASB.

(c) in a June 2013 keynote speech Hans Hoogervorst outlined a ten-point plan to make disclosures more effective.

It's not all talk!

We believe investors should be encouraged by some recent improvements to disclosures:

(a) new pension disclosure requirements can help investors better understand risks surrounding pension liabilities; and

(b) new consolidation disclosure requirements will help investors better understand consolidation and joint venture activities.

We are also undertaking a Disclosure project that will focus on short-, medium- and long-term ways by which we can improve disclosures, including:

(a) changes to accounting policy disclosures and the order of notes;

(b) better disclosure about non-cash changes in debt; and

(c) research on materiality, general disclosure principles and the interaction with existing accounting standards.

How can you get involved?

See our Disclosure Initiative webpage for various ways to keep up to date and stay involved.

Insights on the changes to revenue recognition

The IASB has just revised its Standard for revenue recognition. Investors should expect to see some material accounting restatements when the new Standard is implemented in 2017.[1] In this issue we focus on the investor-relevant aspects of transition. In future editions we will explore the accounting changes in more detail and how they could specifically affect some industries.

It's years away; why should I care?

There are numerous reasons why it makes sense to keep up to speed on any accounting change that is on the horizon. In the case of revenue recognition, however, there is a particularly compelling reason to start conversations with management today.

This is because companies can apply one of two different methods to make the transition to the new Standard. *The transition method they choose may affect the amount of restated historical data that they report to investors*.

Option 1: This approach would give investors at least one year of comparable information (the number of years of restatements will depend on local securities regulation and management discretion).

Option 2: Some companies have suggested that it would be difficult to restate the revenue from some contracts for the prior year. For example, if they have a number of long-term contracts in place then taking Option 1 would require significant judgement—not to mention time and cost.

For that reason, the transition rules allow companies to opt to use the new revenue recognition Standard without providing prior year comparable information.

In such situations, management will be required to provide disclosures that show how revenue would have looked under the old Standard.

What can investors do today?

Now is the ideal time to engage with management about their plans for moving to the new Standard. Make sure you get the information you need!

What will happen to disclosures?

Elsewhere in this newsletter we discuss the IASB's focus on disclosures; revenue recognition is no exception. Examples of the new disclosures that you should see include:

(a) a breakdown of the revenue number, for example, by type of customer or market;

(b) contract balances, including the opening and closing balances of receivables, contract assets and contract liabilities;

(c) information about the judgements used to determine the amount and timing of revenue; and

(d) assets recognised from the costs to obtain or fulfil a contract with a customer.

Which companies will be affected?

Sectors that we expect to be most impacted by the new Standard include: automobile, software and telecommunications.

For sectors selling more straightforward products and services, we don't expect the changes to revenue recognition to affect them much, if at all.

How can I keep in the loop?

The IASB has a programme in place to help stakeholders through the transition to IFRS 15. This includes hosting conferences in which companies share their experiences of the transition, providing investors with insights ahead of the change. Click here to register for investor alerts from eIFRS.

Register here for the free live webcast on Revenue Recognition hosted by the CFA Institute with the IASB and the US national standard-setter, the Financial Accounting Standards Board (FASB).

The webcast will take place on 27 June 2014 at 10 – 11:30am EDT (3 – 4:30pm BST).

[1] The Standard, IFRS 15 *Revenue from Contracts with Customers*, is effective 1 January 2017. Expect financial reports to change with interim reporting in 2017. The first annual reports will be for FY17. Early adoption is allowed.

IASB in profile

Patricia McConnell: IASB member

Every issue we will be featuring IFRS events and/or interviews with key stakeholders or IASB members.

We recently interviewed Patricia McConnell, who will be leaving us at the end of June after five years as an IASB member.

Patricia is a former Senior Managing Director in Equity Research and Accounting and Tax Policy Analyst for Bear Stearns & Co. In a 32-year career in Bear Stearns' Equity Research group, Patricia established herself as one of the leading analysts in the United States on issues related to accounting. *Institutional Investor* magazine ranked her the leading analyst in the US on accounting and tax matters for 16 consecutive years from 1991–2006.

***IASB investor team*: What have been your best memories working at the IASB?**

PM: I think the staff is probably the most competent group of people that I have ever had the pleasure to work with before in my life, and I've worked with a lot of very bright people. They want it [the Standards] to be a good product and they want it to help investors. When you stop and think about how technical this job is (and about how important words are in a Standard), and that many of our staff are working in a language that is not their native language and yet producing these marvellous Standards, you just realise how incredibly talented they are.

***IASB investor team*: What about on the standard-setting front?**

PM: My best standard-setting memory was completing the consolidation Standard [IFRS 10 *Consolidated Financial Statements*] and eliminating what for generations had been a bright line to decide whether or not an entity was controlled. [This] caused a lot of mischief over the years and a lot of confusion. It often made it difficult to compare entities and to really understand what the underlying earnings power was of an organisation, and certainly made it difficult to understand the leverage of the entity.

***IASB investor team*: How has your background helped you in standard-setting?**

PM: I think working at Bear Stearns with both the sell-side and buy-side sector analysts gave me an appreciation for how accounting information is used in the investment community. I think I probably have a different view about what accounting standard-setters should or should not be trying to do to help the investment community. [For example,] sometimes we have to look beyond the KPIs [key performance indicators] that investors use and give them the information that we think they actually need and can use.

***IASB investor team*: What are the big plusses for investors compared to when you began at the IASB five years ago, and what does the future hold?**

PM: The big plus is that there is a single set of global accounting standards. Although IFRS isn't converged totally with the US, it's close. It hasn't even been ten years since Europe adopted IFRS, and now virtually all the world follows it. That is so much better for investors than the situation a decade ago when, for example, every set of financial statements you picked up from Europe was prepared on a different basis and investors really did have huge arguments about which was better. I see as the IASB's mission for the next ten years that it maintains the ground that it's conquered over the last decade.

The investor engagement team wants to thank Patricia McConnell for all of her help and support over the years, especially with investor outreach. We wish her the best for her post-IASB life. We will miss you, Pat!

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Events calendar

IFRS Foundation conferences

23–24 June 2014—London

13–14 August 2014—Johannesburg

6–7 October 2014—Mexico City

IFRS Foundation Trustees meetings

10 July 2014—London

9 October 2014—Mexico City

January 2015—Zurich

Investor outreach events

25 June 2014—Brussels

What role can investors and advisers play in ensuring quality financial reporting?

Hans Hoogervorst will be speaking at this event, which the IASB is jointly hosting with the European Financial Reporting Advisory Group (EFRAG), the European Federation of Financial Analysts Societies (EFFAS), the Association Belge des Analystes Financiers (ABAF) and the Association of Certified International Investment Analysts (ACIIA).

30 June 2014—London

Joint meeting between the IASB's Capital Markets Advisory Committee (CMAC) and the Global Preparers Forum (GPF).

7 July 2014—Brussels

Reflecting dynamic risk management through macro hedging

Martin Edelmann, IASB member, will be speaking at this investor-focused event, which the IASB is jointly hosting with EFRAG.

Webcast with the FASB and the CFA Institute

New revenue recognition rules: what do they mean for investors?
27 June 2014
10–11:30 am EDT (3–4:30 pm BST)
Register here.

Recent events and announcements

Hans Hoogervorst, Chairman of the IASB, delivered the speech 'Charting progress towards global accounting standards' at the IFRS conference in Singapore in May. In his speech, Mr Hoogervorst outlined the current use of IFRS around the world, notably across Asia.

Ian Mackintosh, Vice-Chairman of the IASB, delivered the speech 'The importance and challenges of establishing standards for global finance' at the Manchester Business School in May. The speech set out the importance to global capital markets of a common language for financial reporting, as well as the challenges associated with achieving this goal.

Mr Hoogervorst delivered the speech 'Accounting and moral hazard' at the Ken Spencer Memorial Lecture in Sydney in April. The main theme of the speech was the concept of moral hazard and finance, and what accounting standards can do to prevent it.

The IASB launched the IFRS Research Centre with the aim to facilitate communication between the IASB and the broader research community. It will do this by increasing awareness of the issues that the IASB will be considering in the coming two to three years, encouraging research professionals to undertake targeted research projects and contributing to the IASB moving to more evidence-based standard-setting.

The IASB agreed a charter of mutual co-operation with the accounting standard-setting community. The charter establishes key principles of co-operation between the IASB, national standard-setters and other accounting standard-setting bodies, represented by the International Forum of Accounting Standard Setters (IFASS).

The IFRS Foundation published its Annual Report for the year ended 31 December 2013. The Annual Report provides an overview of the IFRS Foundation's activities, highlighting the progress made towards establishing IFRS as the single set of high quality, globally accepted accounting standards.

In April 2014, the Trustees held their quarterly meeting in Sydney. A summary of the meeting is available here.

Contact us

For more details on any of the events or announcements mentioned, or for any other information, please email Barbara (bdavidson@ifrs.org) or Fred (fnieto@ifrs.org).