A number of documents and proposals have been released over the past two months. This issue of Doctr’in includes the latest provisions from the IFRIC on employee benefits and the EFRAG proposal on revenue recognition. In addition, with the approach of year end, several Q&As will help you addressing the first application of IFRS 7. Finally, Doctr’in offers an overview of the first application of the US GAAP FIN 48 interpretation and the prospects for IFRS accounts.

Michel Barbet-Massin   Jean-Louis Lebrun

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**News**

**IFRS & SMEs**

The IASB has decided to postpone the deadline for comments on the exposure draft on IFRS for SMEs to November 30, 2007. This delay aims to provide companies involved in “field tests” with enough time to finalise their work.

Doctr’in will publish the main comments from Mazars in its response to the request for comments.

**Former Prime Minister and Finance Minister of the Netherlands becomes Chairman of the IASCF Trustees**


**EFRAG comments on the “insurance contracts” discussion paper**

The EFRAG published its provisional comments on the recognition of insurance contracts on October 3, 2007. The EFRAG considers the document to be a satisfactory basis on which to launch the debate.

**“Insurance” working party seeks candidates**

The IASB is looking for one or two people with practical experience in the use and interpretation of financial information by insurance companies. These two candidates will join the working party created in 2004 to provide an opinion on the “Insurance Contract” project. The first meeting is scheduled for the second quarter of 2008.
Elimination of proportionate consolidation: release of the exposure draft

The IASB published the ED 9 – Joint arrangements exposure draft on September 13, 2007. This draft standard aims to replace IAS 31 on interests in joint arrangements and assets and operations under joint control. It is in line with the IASB and FASB convergence project.

The IASB’s proposal introduces two major changes to the current standard, mostly applying to joint ventures:

- The legal form of the agreement between the entities is no longer the main factor determining the choice of accounting treatment, and
- The proportionate consolidation accounting option is eliminated.

According to the IASB, the amended standard will better meet the quality and comparability requirements of IFRS financial statements. The accounting treatment must indeed take account of the legal form of the agreement but also of the rights and obligations of each party. Taking them into account will make it possible to better reflect the economic outcome of the arrangement.

The IASB considers that proportionate consolidation does not properly reflect the economic outcome under this recognition method. An entity may recognise assets that it does not control. Thus when an entity recognises outcomes related to its interest in a joint arrangement, it may not be entitled to use those outcomes alone. They do not therefore meet the definition of assets as expressed in the current version of the Conceptual Framework.

Comments on ED 9 should be submitted to the IASB by January 11, 2008. Mazars’ comments on this exposure draft will be included in a future issue of Doctr’in.

Presentation of the revised IAS 1

The revised IAS 1 - Presentation of Financial Statements – was published on September 6, 2007 by the IASB. It finalises Phase A of the “Performance Reporting” project and its application will be compulsory from January 1, 2009 (early application is encouraged).

The revised IAS 1 introduces the fundamental concept of “comprehensive income”, which is already included in US GAAP. What is the “comprehensive income”, or “statement of recognised income and expenses”? It is a specific statement including:

- The net result, as currently calculated; and
- The “other recognised income and expenses” (or comprehensive income), including:
  - the actuarial gains or losses on defined benefit schemes subsequent to employment (in line with paragraph 93A of IAS 19);
  - fair value variations in securities recognised as held for sale (IAS 39);
  - the efficient part of fair value variations in hedging instruments within a cashflow hedging (IAS 39),
  - foreign exchange differences.

What are the major changes to the current IAS 1?

- The detailed presentation of other income and expenses recognised directly in equity:
  - either within the income statement (a single statement), which is the IASB’s preferred solution;
  - or in a separate statement (the current “SORIE” - Statement of Recognised Income & Expense), presented in a distinctive document from the variations in equity schedule, which should, in future, only include the details of the outcome of transactions with shareholders;
The obligation to provide an opening balance sheet for the first comparative period in the case of reclassification or retrospective retreatment (i.e. in line with IAS 8);

The obligation to detail, in the notes, the amounts related to other income and expenses recognised through profit or loss (for example, in the case of disposal of securities held for sale) and the tax impact on each component of other income and expenses;

The change in the name of the most commonly used financial statements (not compulsory). The balance sheet may be renamed the “statement of financial position” and the income statement may be renamed as “statement of comprehensive income”.

And then…? Phase B of the project, more fundamental, is expected to lead to the publication of a discussion paper by the end of 2007. This document will provide an overall response to the issue of the presentation of financial information within financial statements in order to improve user comprehension.

Amendment to IAS 39 – hedged risks and portions

On September 6, 2007, the IASB published an amendment to IAS 39 that aimed at clarifying:

- The risks that qualify for hedging;
- The portions of the cashflows for which a hedge relationship may be defined.

The draft amendment proposes to limit the hedged risks to interest rates, foreign currency, credit and prepayment risks. The risks associated with the contractually specified cashflows of a recognised instrument may also be hedged. For example, the inflation risk inherent in a loan whose remuneration is equal to the inflation rate + 200bp could be hedged. However, the commodities price risk is not explicitly mentioned.

The IASB also proposes to clarify the portions of financial instruments that qualify for hedging. These portions must be identified in accordance with the following criteria:

- duration: part of the instrument’s time period to maturity may be hedged;
- proportion: a percentage of the cashflows of the instrument may be designated as a hedged item;
- upward or downward hedging: the cashflows of the instrument, if the risk rises or falls beyond a reference value (for example, the foreign currency risk for an order of 1 000 USD if the US Dollar is below 0.7 EUR);
- independence between cashflows: all cashflows that are independent of the others may be hedged separately (for example, the first three interest payments on a loan);
- the reference rate: the portion of the cashflows of an interest-bearing financial instrument that is equivalent to a risk-free rate or a reference rate (for example, the Euribor component of a Euribor + 120bp liability may be hedged).

Comments may be submitted to the IASB by January 11, 2008.

IFRS consolidation scope and non-significant entities

The publication of consolidated accounts is compulsory even if the parent company controls non-significant entities.

This position has been confirmed by the European Accounting Regulatory Committee (ARC) in a meeting held in June. Following an analysis of the potential conflicts between the 4th and 7th accounting Directives (which set out exemptions to the provision of consolidated accounts) and Regulation 1606/2002/EC on the adoption of IFRS standards in the European Union, the ARC concluded that there were no possible exemptions, relating to the relative size and materiality of subsidiaries of the group, to the requirement to provide consolidated accounts compliant to IFRS rules.
In practice, a company that is not publishing consolidated accounts because it does not cross the statutory thresholds would not be able to use this argument when complying with IFRS. The scope of consolidation must thus be determined in accordance with IAS 27, IAS 28 and IAS 31.

If, because of the application of the materiality principle existing in the Conceptual Framework, the scope of consolidation only includes the parent company (the subsidiaries being non-significant), IFRS compliant accounts will nevertheless be named “consolidated accounts”.

This response is of particular interest to companies which did not previously publish consolidated accounts and which issue debt securities on a regulated market of a Member State. Such entities must publish consolidated accounts under IFRS standards from January 1, 2007, even if their subsidiaries are non-significant.

**Revenue Recognition**

The Board had not considered this project for more than a year. The decision had been now taken to develop two models on a separate basis (the “fair value” model and the “customer consideration” model), to be drafted by two different IASB-FASB joint working parties.

Staff presented the progress of the work to the two Boards at the joint meeting in October.

IASB members still seem far from an agreement on this subject. In the meantime, however, it should be noted that the broad lines of the “fair value” model have been implemented in the IASB’s proposals on insurance contracts.

**Fair value measurement provisions**

The Board received the analysis of the comments on the Discussion paper published at the end of 2006 and approved the working schedule proposed by staff. The objective is to publish an exposure draft during the third quarter of 2009, after several round tables to be held in April 2008. The main objective of these round tables will be the testing of the results of the Board’s initial discussions.

**IASB - EFRAG “Convergence” meeting**

Over the last two years, the IASB and the EFRAG have been meeting twice yearly in order to enable Europe to express its own opinions and views on current projects, in particular the joint projects conducted by the IASB and the FASB, through the EFRAG.

At the meeting on October 15, 2007, the EFRAG
- questioned the IASB on the allocation of priorities between the various projects,
- recommended that the interaction between the development of new projects and the review of the conceptual framework be addressed in a different order.

The delegation present in London again indicated that the publication of the revised IFRS 3 and IAS 27 could raise issues in Europe, without pre-judging the future EFRAG recommendation or the adoption process.
“Customer contribution”

In September 2007, the IFRIC continued its deliberations on the accounting treatment of contributions from customers to service providers such as energy providers (electricity, gas, water) and telecommunication providers (telephone, internet access, digital television…).

The issue relates to the method of recognition in the service provider’s statements of contributions related to the building or the financing by a client of an infrastructure (asset) allowing access to the network of a service provider.

According to IFRIC current discussions, an entity receiving a contribution should recognise an asset if the contribution meets the definition and the criteria for the recognition of an asset (the resource in question generates future economic benefits for the entity). The asset would be measured at fair value as the counterparty to a liability representing the obligation of the provider to supply the service. This liability would be recognised in profit or loss during the period in which the provider uses the asset to provide the service to the customer.

In addition, the IFRIC has stated that this treatment, which was initially related to the use of a physical asset, would also apply to contributions in cash.

A draft interpretation is expected to be available shortly.

CNC comment letter on D21

On October 1, 2007, the French standards body, the Conseil National de la Comptabilité (CNC), published a comment letter on the D21 draft interpretation on real estate sales.

While the CNC supports the IFRIC proposal to clearly identify the standard applicable to real estate sales, it raises the attention of the IFRIC to the potential impacts of the draft on the other industries. The CNC asks the interpretation committee to clarify whether the draft should be applied by analogy to all industries.
European matters

Has the adoption of IFRS 8 been saved by the European survey?

IFRS 8, “Operating segments”, was published by the IASB on November 30, 2006 and is intended to replace IAS 14 on segment reporting. Despite approval from the EFRAG and the ARC, the European Parliament has blocked the adoption process for this new text. Against this background, the Commission had launched a survey on the consequences of IFRS 8 implementation for companies (refer to the May 2007 issue of Doctr’in).

The European Commissioner Charlie McCreevy presented a summary of this survey to the European Parliament on September 11, and recommended the adoption of the text, on the basis of the 200 questionnaires received. He insisted in particular on the need to deliver a clear message to companies wishing to implement the text early (i.e. before January 1, 2009).

IFRS 8 introduces the “management approach”: the information is presented according to the segmentation used by the management. IAS 14 applies segmentation based on the risks and profitability of the segments. In addition, as opposed to IAS 14, IFRS 8 does not require the presentation of segment data under IFRS (it nevertheless requires a reconciliation with the consolidated accounts). The Parliament had blocked the adoption process due to the risk of lack of comparability incurred by the implementation of IFRS 8.

Charlie McCreevy’s speech is a step towards the adoption of IFRS 8 by the European Union. However, it does not presage the decision of the Parliament, whose role has recently been strengthened (see the April 2007 issue of Doctr’in). The new standard could therefore be adopted in October 2007 at the earliest. If not, the IFRS basis “as adopted by the European Union” would be significantly different from the IFRS basis as published by the IASB from 2009.

At a time when the SEC is proposing to eliminate the obligation to reconcile financial statements drawn up under IFRS with those produced under US GAAP for foreign companies listed in the United States, might this lead the US market regulator to reconsider its proposal?

European Commission expresses concerns regarding IFRS for SMEs

On February 15, 2007, the IASB published an exposure draft on IFRS for SMEs (see the February 2007 issue of Doctr’in) proposing a simplified version of the IFRS standards for these companies. However, the European Union believes that the proposed standard remains too complex.

The goal of the IASB is to create a full set of simplified accounting principles that may be used by unlisted companies. This objective of simplification might have appealed to the European Commission, which aims to reduce the administrative burden on SMEs.
However, on his speech of September 13, 2007, European Commissioner Charlie McCreevy expressed concerns regarding the IASB draft, saying that the proposals were insufficiently simplified.

For this reason, the Commission does not plan to require the European Union to adopt the draft at this stage. In addition, the Commission appears convinced that this draft does not comply with the 4th and 7th Directives, a situation which would prevent any member of the European Union from applying the IFRS standard for SMEs.

The deadline for the submission of comments, initially set at October 1, 2007, has been postponed to November 30, 2007. The final standard is expected in the second quarter of 2008.

Finally, it should be noted that, for the first time, the IASB has published official translations of the exposure draft in French, German and Spanish. They are available on the Internet site www.iasb.org.

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Presentation and publication of the ICAEW report on the implementation of IFRS in Europe

The European Commission asked the Institute of Chartered Accountants in England and Wales (ICAEW) to conduct a survey on the implementation of IFRS in Europe in 2005. The results of this survey were revealed during a presentation in Brussels on October 18, 2007.

The survey, conducted on the basis of a sample of 200 annual reports and various interviews and round tables, has concluded that the implementation of IFRS standards in Europe is satisfactory.

However, the authors of the survey state that there is still room to improve the quality (and the compliance level) of the notes to the accounts.

The detailed report, now available on the website of the European Commission, is very interesting. Doctr’in will report its main provisions in a future issue.

News in brief

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The detailed report, now available on the website of the European Commission, is very interesting. Doctr’in will report its main provisions in a future issue.
In July 2007, the IASB published IFRIC 14 on the mechanism for limiting a defined benefit asset and on the introduction of prudential requirements on the financing of pension schemes in a number of countries.

The implementation of IFRIC 14 is compulsory for annual periods starting on January 1, 2008, while an early application is encouraged.

Why the limit?

In practice, certain post-employment benefit schemes are pre-financed. The employer decides to dedicate assets to cover the liabilities, through the subscription of insurance contracts or through specific entities such as pension funds. From a legal point of view, these assets cannot be recovered by the employer or be used in favour of a creditor: they may only be used to finance the post-employment benefit scheme, in line with the purpose of the insurance contract or the statutes of the specific entity.

Because of the uncertainties to which both the liabilities and assets are subject, the scheme may experience a surplus. The issue is therefore to what extent an asset may be recognised in the balance sheet of the company. The restrictions on these assets do not entail the loss to the employer of all future economic benefits derived from the surplus; the surplus may be used, provided that it allows a reduction of future contributions or the financing of new rights.

IAS 19 therefore provides for the recognition of a defined benefit asset, within the limits of the future economic benefits for the company. The limit rule therefore makes it possible to avoid the recognition of an asset which would not provide any future benefit for the company. The limit rule set out under IAS 19 was amended in 2002, as its implementation could have led to anomalies due to the existence of deferred recognition mechanisms for a number of accounting items. Indeed, the implementation of the rule prior to 2002 could have led to the recognition of a profit due to the occurrence of actuarial losses, as the actuarial loss resulted in a reduction of the surplus and therefore decreased the impact of the limit rule, while its recognition was deferred using the corridor mechanism.

What does IFRIC 14 bring?

While the 2002 amendment improved IAS 19 by preventing the recognition of a profit (or a loss) resulting only from the occurrence of an actuarial loss (or profit) through the limit rule, it did not provide any additional guidance on the practical implementation of this complex rule.
IFRIC 14 made it possible to clarify:

- the implementation procedures for the limit rule, including the determination of the existence of a future economic benefit related to a surplus,
- the interaction of the limitation rule with the regulatory constraints for post-employment benefit schemes, which are common in certain countries,
- the criteria for the existence of a potential liability resulting from regulatory constraints on the financing of the schemes.

**Determining the existence of a future economic benefit**

Whether the entity is able or not to realise immediately an economic benefit does not predict the existence of this economic benefit. The criteria are:

- the capability of the company to create it in the future,
- the absence of any condition for its realisation which could not be controlled by the company.

The amount of the economic benefit must be assessed:

- by deducting the potential costs related to its realisation,
- on the basis of scenarios compatible with the scenarios used to assess the liabilities of the pension scheme,
- assuming a stable population within the scheme, unless the company has undertaken to reduce staff.

**The impact of regulatory constraints on the financing of the scheme**

A company must distinguish between:

- the contributions required by the regulation to cover a current deficit:
  - If these contributions are "recoverable" in the future (as reductions of future contributions or through reimbursement of the fund), the company shall not recognise a liability or reduce the pension asset because of this constraint;
  - In the opposite case, the recognised liability (or asset) should be increased (or decreased) to avoid any gain or loss due to the implementation of the limitation principle when the contributions are paid;
- The contributions required by the regulation to cover the future acquisition of rights. The company must calculate the economic benefit as the current value of the difference between:
  - the forecast cost of the services provided during the period in future years, and
  - the forecast of the minimum contribution flows caused by the regulatory constraint.
Should we expect changes in the recognition of revenue?

Since the introduction of the IFRS in 2005, companies have experienced a period of stability in the standards. However, the IASB remains active and is preparing number of drafts for the revision of current standards. One of them addresses the recognition of revenue. Under the current agenda, a first draft is expected to be published in 2008, with the publication of the final standard in 2010.

In such a context, Europe (through the EFRAG), published a document on revenue recognition in July 2007, in order to contribute to the work of the IASB.

Why change the existing standards?

The objective of the EFRAG is to keep a single approach to the recognition of revenue, applicable whatever the transaction and the sector.

Currently, two standards address the recognition of revenue:

- IAS 18 “Revenue” sets out the treatment of revenue from ordinary activities related to the sale of goods, the provision of services, interests, royalties and dividends;
- IAS 11 “Construction contracts” sets out the treatment of revenue and costs related to construction contracts in the financial statements of the builder.

For example, in the case of the sale of goods, revenue is recognised when the company has transferred almost all the risks and rewards of ownership of the assets to the buyer. It is therefore necessary to determine the event that generates the transfer of the risks and rewards, which generally takes place on the transfer of ownership in the simplest cases. Under this approach based on the “critical event”, revenue is recognised only when the seller has met all its obligations towards the buyer.

In the cases of services or construction contracts, the revenue is recognised under the percentage of completion method. According to this method, the revenue is recognised on an ongoing basis as the seller’s work progresses in a “continuous approach”. Progress is usually calculated by comparing the work done at the relevant date with the total estimated amount of work.

As a consequence, for transactions concluded over time in particular, the recognition of revenue under the “continuous approach” takes place earlier than when using the “critical event” approach.

According to the EFRAG, the existence of two approaches for revenue recognition is questionable in the two following situations:

- when it is difficult to know whether a sale falls under the scope of IAS 18 or IAS 11. This is the case for certain construction or real estate development contracts. This issue is being analysed by the IFRIC (IFRIC D21 - Real estate sales).
- when the sales are complex transactions that include a number of components. In these cases, it is sometimes difficult to know whether the transaction should be broken down in several components to implement the revenue recognition criteria.
In these two situations, the recognition of the revenue may vary:

- depending on the standard used: IAS 18 ("critical event" approach) or IAS 11 ("continuous approach"); the revenue is recognised earlier if IAS 11 is applied;
- If IAS 18 is used, depending on how the transaction is broken down into components, the revenue being recognised much sooner when a large number of components are identified.

The examples analysed by the EFRAG to compare the two approaches

The EFRAG illustrated its arguments with five examples:

- The sale of a manufactured chair, taken and paid for immediately by the customer;
- The sale of a washing machine installation service by a plumber, to be paid for by the client once the work is complete;
- The sale of a cleaning service for premises every evening during one year, invoiced monthly;
- The sale of a construction contract for a bridge according to the customer’s specifications, the construction being done in three phases, each of them being subject to a separate invoice (total duration: three years);
- The sale of a computer equipped with specific software, the vendor being committed to the installation of the computer and to the provision of 10 hours’ training. The goods and the installation are billed separately from the training service.

"Critical event" approach

The "critical event" approach can be applied in three ways.

**Option 1**

Revenue is recognised only when the provider has fulfilled all his obligations. This option provides satisfactory results for simple transactions, such as the sale of a chair or the installation of a washing machine. However, in the other cases, the revenue is recognised very late, when all the work is complete, which is not satisfactory for long term contracts in particular (cleaning service, construction of the bridge, sale and installation of computers followed by user training).

**Option 2**

Revenue is recognised when the provider has fulfilled part of his obligations and is entitled to be paid for the performance of his obligations. In this case, sales are broken down into several components, each component entitling the seller to invoice the customer and leading to the recognition of part of the revenue. This option allows an earlier recognition of the revenue than the first option:

- Cleaning service: recognition of revenue on a monthly basis;
- Construction of the bridge: recognition of revenue at the end of each of the three phases;
- Sale of computers: recognition of revenue in two phases (at the end of installation and at the end of training).

According to the EFRAG, the disadvantage of this option is that it relies upon the terms of the contract. This could lead to different recognition methods for transactions with similar economic purposes, depending on the terms and the legal environment of the contract.
Option 3

Revenue is recognised when the provider has fulfilled part of its obligations and the work done corresponds to a component of the contract which has a specific value for the client. In this case, the sales are broken down in several components which have a value for the client, each of them resulting in the recognition of part of the revenue. This third option also allows a quicker recognition of the revenue than option 1, and potentially than option 2. However, according to the EFRAG, this option is subjective and may be complex to implement.

The “continuous approach”

The continuous approach consists in the recognition of revenue on an ongoing basis, as stated in IAS 11, i.e. according to the percentage of completion. Its advantage is that it depends on the determination of the work done by the provider and not on the obligations of the seller or on the terms of the contract. This approach allows the gradual recognition of revenue over the duration of the contract. Thus in the case of the sale of the chair or the installation of the washing machine, it provides the same result as the “critical event” approach, i.e. the recognition once the work is done (the work being done over a very short period of time). However, it allows an earlier and more gradual recognition of the revenue in the other cases, as and when the work is carried out.

Which method of revenue recognition for the future?

The EFRAG has not provided a recommendation for the use of one method or another. However, it considers that a single homogeneous approach should be adopted for the recognition of revenue. The EFRAG notes that the continuous approach appears easier to implement, especially for complex transactions or transactions with multiple components.

If this approach gains ground and is used for all transactions, including those currently under the scope of IAS 18, revenue could be recognised earlier, in particular for sales of goods under a firm order. In practice, revenue would be recognised on an ongoing basis according to the percentage of completion and not at the date of delivery. However, this recognition could raise practical difficulties which remain to be analysed.

Comments may be sent to the EFRAG until 10 December 2007. Brainstorming on this subject has only begun …
Focus Studies

First application of FIN 48: US GAAP and prospects for IFRS accounts

The FASB published interpretation FIN 48 on FAS 109 on income tax in 2006. This interpretation, Accounting for Uncertainty in Income Taxes, addresses uncertain or aggressive tax positions. French groups listed on the NYSE will be subject to the requirements of this interpretation for the first time for annual periods ending on 31 December 2007. In addition to the provisions applicable to these specific groups, this interpretation indicates the direction of the future IAS 12, for which an exposure draft will be published during the first quarter of 2008. The review of IAS 12 reflects the aim of achieving the short term convergence of IFRS and US GAAP.

Recognition principles under FIN 48

The FIN 48 interpretation aims at clarifying the treatment of uncertain tax positions (for income tax only), such as the decision to reduce specific expenses, not to recognise certain income or not to submit tax forms, etc. The interpretation also strengthens the level of information on tax risks provided in the notes to financial statements.

The FASB’s interpretation presents a two-stage methodology. The first aims at justifying the recognition of the tax benefit, while the second addresses the measurement of the tax benefit to be recognised.

Phase 1: recognition of the tax benefit related to an uncertain tax position

The company can recognise the economic benefits of the adopted tax position only if it is “more likely than not” that the tax position will be accepted by the tax authorities, on the basis of texts, case law, practice or following a decision from the relevant court of last resort.

Phase 2: measurement of risks resulting from the uncertain tax position recognised in the first phase

If the tax position complies with the recognition criteria provided in the first phase, the company must estimate the amount of tax benefit to be recognised. The tax benefit to be recognised is limited to the highest amount with a cumulative probability above 50% of acceptance by the tax authorities (cumulative probability concept). It should be noted that the company must also make provision for the interest and penalties relating to tax positions not recognised in the result.
**Practical example**

A company has taken a tax position incurring a tax benefit of 100.

**Phase 1:** the analysis concludes that the tax position complies with the recognition criteria under FIN 48.

**Phase 2:** measurement and recognition of the tax benefit.

On the basis of the following table, the entity determines the highest amount with a more than 50% probability of acceptance by the tax authorities:

<table>
<thead>
<tr>
<th>Expected benefit following agreement with the tax authorities</th>
<th>Occurrence probability</th>
<th>Cumulated occurrence probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>100</td>
<td>2%</td>
<td>2%</td>
</tr>
<tr>
<td>80</td>
<td>45%</td>
<td>47%</td>
</tr>
<tr>
<td><strong>60</strong></td>
<td><strong>15%</strong></td>
<td><strong>62%</strong></td>
</tr>
<tr>
<td>50</td>
<td>15%</td>
<td>77%</td>
</tr>
<tr>
<td>40</td>
<td>8%</td>
<td>85%</td>
</tr>
<tr>
<td>20</td>
<td>8%</td>
<td>93%</td>
</tr>
<tr>
<td>0</td>
<td>7%</td>
<td>100%</td>
</tr>
</tbody>
</table>

The company recognises a tax benefit of 60 (while the tax declaration recognises a benefit of 100) as a counterparty for a tax debt of 40 (100-60). If necessary, provision must be made for interest and penalties.

An analysis of the tax position must be carried out when it is first ascertained. It must be reviewed subsequently in the following cases:

- The recognition criterion, which was not met originally, is now met;
- The position has been the subject to an agreement with the authorities or of a definitive judgment;
- The tax position can no longer be reversed by the tax authorities.

This interpretation stresses the information to be provided in the notes:

- The amount of the unrecognised tax positions at the date of opening and closing, as well as the detailed movements over the year by category;
- In the case of tax positions for which the amount of unrecognised benefits could vary over the next 12 months, the nature of the uncertainty, the event that would give rise to the change and the extent of the expected variations.

In addition to the recognition and measurement provisions for the tax positions adopted by companies, the obligation for them to document and publish such information remains highly controversial. Companies fear that this "sensitive" information may be used by the relevant tax administrations for their tax audits.

Companies are all the more worried that, under the Sarbanes Oxley Act, they must establish a formalised procedure to allow the identification of uncertain tax positions and procedures for recognition and measurement (case law, external tax lawyers’ opinions etc.)

Despite the criticisms from those preparing accounts, inter alia regarding the confidentiality of information vis-à-vis the tax authorities, the FASB has declined to postpone the application of this interpretation.
Discrepancies between IFRS and US GAAP

For those preparing financial statements under US GAAP in France, the issue of convergence in terms of the recognition and measurement of uncertain tax positions is crucial, not least because it is difficult for them to express discrepancies on this subject to the market.

Under current IAS 37, a company must set aside provision when it is probable that the obligation will incur an expense for the entity. The word “probable” seems similar to the wording of FIN 48 “more likely than not”, but it does not apply to the same stage of the analysis. Under FIN 48, the analysis is made on the assumption that the entity will be subject to a tax audit, while IAS 37 includes the probability of a tax audit within the overall probability of an expense for the entity. Thus:

- Tax benefits could potentially be unrecognised under FIN 48 (because it is probable that they would not be accepted by the tax authorities in the event of an audit), while the corresponding tax benefit could be partially or fully recognised under IFRS;
- Tax benefits might be only partially recognised under FIN 48, but fully recognised under IFRS.

In addition, where FIN 48 and IAS 37 require provision, the method of estimating this provision is different. IAS 37 requires the liability to be assessed at the most likely expense, possibly adjusted for the other scenarios with a significant occurrence probability.

In the example above, under IFRS the company would make a provision of 20 based on the most likely scenario (or 30 when taking into account the other scenarios with an occurrence probability of more than 10%), while a provision of 40 would be required under FIN 48.

Impact on revised IAS 12

The FASB and the IASB plan to revise IAS 12 and FAS 109 under a joint project aiming to achieve convergence. At this stage, the discussions between the two standards bodies suggest that their positions are still some way apart.

- Under IFRS, uncertain tax positions would be taken into account according to the provisions of the future IAS 37 on the recognition of liabilities, and measured using the expected value method. In addition, the IASB is considering provisions on the information to be given in the notes;
- Under US GAAP, the measurement principles defined by FIN 48 would be changed, in order to make a provision corresponding to the most likely result (“single point best estimate”).
IFRS 7, a financial information standard on financial instruments, must be applied for annual periods beginning January 1, 2007. On the eve of the first implementation of this new standard, we draw your attention to several critical aspects and difficulties of application observed in practice.

**Everyone is concerned**

The IFRS 7 standard is applicable to all companies, whatever their sector of activity. It requires two types of information:

- The weight of financial instruments in the financial position and performance of a company,
- Qualitative and quantitative information on exposure to risks related to financial instruments.

**The major difficulty is the quantitative information on risks!**

**Credit risk**

More detailed information must be provided on credit risk. The purpose of this information is to allow the user of the financial statements to determine the exposure of the company to credit risk and the way it manages this risk. With this in view, IFRS 7 requires the publication of:

- An analysis of the age of past due but not impaired loans
- An estimate of the fair value of guarantees

This information is of direct concern to financial institutions. However, it should cause industrial and service companies to publish the historical statement of client accounts receivables on a consolidated basis, as client accounts receivables are financial assets! In addition, this is a somewhat specific historical statement as it only includes the past due but not impaired loans and receivables.

**Liquidity risk**

A schedule of financial liabilities by maturity must be provided. It includes non-discounted contractual cashflows. In practice, this schedule must include:

- For non-derivative liabilities, capital and also interest flows.
- For derivative instruments resulting in an exchange of the notional amount between the parties (cross currency swaps for example), the notional amount, since it results in an expense. In order to produce relevant information, this flow has to be completed showing the parallel flow received as counterparty.
- For derivatives not resulting in an exchange of the notional amount but with a negative value at year end, the future net flows must be broken down in the schedule (it is possible that some of these net flows will be positive over certain periods).

Taking into account only the derivatives with a negative fair value (i.e. financial liabilities) at year end does not provide fully relevant information: it is therefore useful to integrate all the derivative positions (with negative or positive fair value) in the maturity table.
This information may be completed with a schedule including also the financial assets. This schedule would be based on
the estimated dates of cashflows and not on the contractual maturity of the instruments. This information is more
representative of the way a company (a financial institution in particular) manages its liquidity risk.

Market risks
The standard requires a sensitivity analysis for all market risks (rates, foreign currency, equities, commodities etc.) to which
the entity is exposed. The standard does not require a specific method for the measurement of sensitivity. When a group
uses tools such as the value at risk for the monitoring and management of these risks, it may use that information as a
basis for the financial information.

If the company has not introduced such tools, the aim is to provide quantitative information on the impact of a possible
variation of the component on the result and the share capital.

The sensitivity analysis should be carried out on the basis of the existing portfolio at the date of closure, without
recalculating what the result would have been if the component had varied during the year. This approach assumes
that the situation at year end is representative, for example of the interest rate risk, the net indebtedness, the breakdown
between fixed and floating rates and the currencies in which the debt is denominated. If this is not the case, the
standard states that a different approach may be used, provided that the reasons why the situation at year end is not
representative are mentioned.

While companies have a certain level of freedom in the measurement of sensitivity, they must account for the methods
and hypothesis used and for changes between one period and another.

Finally, it should be noted that this information can be presented separately from the financial statements, in a business
report for example, but that it remains subject to inspection by the auditors.
Technical support daily life

Issues most frequently raised with the Technical support department

- Treatment of EPS increases/decreases related to the purchase or sale of equities;
- Recognition of a business combination: analysis of a Purchase Price Allocation;
- Increase of interest percentage in a controlled entity;
- Accounting treatment of sponsorship agreements (off balance sheet liabilities or liabilities in the accounts of the sponsor) and of corresponding tax benefits;
- Does a factoring contract between a company and a bank result in the de-recognition of the loans sold?
- How to recognise a commitment to repurchase minority interests when the price is paid partially in cash and partially in the securities of the parent company which carries out the repurchase?
- IFRS 5: initial and post measurement;
- How to recognise an issuance of subscription right certificates whose exercise price is below the market price of the underlying stock at the date of issuance and which is subject to an exercise and placement guarantee from banks?
- Combination of businesses under joint control;
- Transfer of assets between entities controlled by the State, measurement of the contributions in the individual and IFRS accounts;
- Method for margin recognition in a construction contract, treatment of financial expenses;
- Accounting treatment of the internal result of the disposal of securities within an M&A deal;
- Creation of a joint venture and use of the “fresh-start method”;
- How to present the impact of texts which have not been subject to an early application on the financial statements;
- Renegotiation of a put granted to shareholder managers;
- Recognition of bonds convertible in equities under IFRS;
- Provision to be made under IFRS for the compensation payable to a provider following the non-realisation of contractual obligations;
- Provision to be made for a loss-making contract;
- Date for taking into account the revenue on allotment operations in IFRS accounts.

Calendar of upcoming meetings of the IASB, the IFRIC and the EFRAG

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