International Accounting Standards Board®

Press Release

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IASB publishes convergence proposals on the accounting for liabilities and restructuring costs

The International Accounting Standards Board (IASB) today published for public comment proposed amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* (to be retitled *Non-financial Liabilities*) and complementary limited amendments to IAS 19 *Employee Benefits*.

The amendments to IAS 37 would require entities to recognise in their financial statements obligations that satisfy the definition of a liability in the IASB's *Framework*, unless they cannot be measured reliably. Uncertainty about the amount or timing of the economic benefits that will be required to settle a liability would be reflected in the measurement of that liability instead of affecting whether it is recognised. This change would enhance financial reporting because some liabilities previously only disclosed in the notes to the financial statements will now be included in the balance sheet. These proposed amendments to IAS 37 complement the Exposure Draft of Proposed Amendments to IFRS 3 *Business Combinations*, which the IASB has also published today, and would result in items previously described as 'contingent liabilities' being treated more consistently in and outside a business combination.

The proposals also mark another step towards convergence of international and national standards by continuing the IASB's work in its joint short-term convergence project with the US Financial Accounting Standards Board (FASB) to reduce differences between the IASB's International Financial Reporting Standards (IFRSs) and US generally accepted accounting principles (GAAP). Specifically, the proposals would align the accounting in IASs 37 and 19 for costs typically associated with restructuring an entity with the requirements of FASB Standard SFAS 146 *Accounting for Costs Associated with Exit or Disposal Activities*. The proposals would require liabilities for costs associated with a restructuring—for example, termination benefits—to be recognised only when the IASB's *Framework* definition of a liability is met. This would improve the comparability and representational faithfulness of

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financial information because like transactions would be accounted for similarly regardless of whether they are associated with a restructuring. More generally, the amendments would align the recognition principles in IAS 37 with those in more recent FASB standards on liabilities.

Introducing the proposals, Sir David Tweedie, IASB Chairman, commented:

> The publication of the proposals to revise IAS 37 continues our work to eliminate major differences between IFRSs and US GAAP and improve our Standards. With these proposed amendments we have adopted principles from recent FASB standards on liabilities and used them to update our general standard on liability accounting. In particular we are proposing to require some liabilities previously described as contingent liabilities to be included in the balance sheet itself rather than only disclosed.

The joint convergence project is expected to result in several more standards. The FASB has recently published standards on exchanges of non-monetary assets and accounting changes and error corrections. On each of these subjects the FASB has converged with improvements made to IFRSs by the IASB in 2003. Further exposure drafts from both boards are expected over the next year, covering segment reporting, income taxes and earnings per share. More information on the short-term convergence project is given on the IASB's Website (www.iasb.org) and the FASB's Website (www.fasb.org).

The IASB invites comments on the Exposure Draft by 28 October 2005.

The primary means of publishing proposed standards and amendments to standards is by electronic format through the IASB's subscriber Website. Subscribers are able to access the Exposure Draft published today through 'online services'. Those wishing to subscribe should contact:

> IASCF Publications Department, 30 Cannon Street, London EC4M 6XH, United Kingdom. Tel: +44 (0)20 7332 2730 Fax: +44 (0)20 7332 2749 email: publications@iasb.org Web: www.iasb.org

Printed copies of the Exposure Draft of Proposed Amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and IAS 19 *Employee Benefits* (ISBN 1-904230-91-1) will be available shortly from IASCF Publications Department.

From 11 July, the text of the Exposure Draft will be available freely from the IASB's Website.

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NOTES TO EDITORS

About the Exposure Draft

The main proposals are as follows. The Exposure Draft:

- clarifies that IAS 37, except in specified cases, should be applied in accounting for all non-financial liabilities that are not within the scope of other International Financial Reporting Standards (IFRSs). To emphasise this point, the Exposure Draft does not use the term 'provision' to describe liabilities within its scope and instead uses the term 'non-financial liability'. However, entities may describe some classes of non-financial liabilities as provisions in their financial statements.

- eliminates the terms 'contingent asset' and 'contingent liability' from IFRSs. The Exposure Draft explains that many items previously described as contingent assets or contingent liabilities satisfy the definition of an asset or liability in the IASB *Framework*. This is because the contingency does not relate to whether an asset or a liability exists. Rather, it relates to one or more uncertain future events that affect the amount of the future economic benefits embodied in the asset or that will be required to settle the liability.

- amends IAS 38 *Intangible Assets* so that items previously described as contingent assets that satisfy the definition of an asset are within its scope rather than the scope of IAS 37. This results in such items being recognised separately from goodwill in a business combination if they satisfy the identifiability criterion in IAS 38.

- omits the probability recognition criterion from IAS 37 (paragraph 14(b)) because in all cases an item satisfying the definition of a liability meets the criterion. Accordingly, the Exposure Draft requires a non-financial liability to be recognised unless it cannot be measured reliably. Uncertainty about the amount or timing of the economic benefits that will be required to settle a non-financial liability is reflected in the measurement of that liability rather than affecting whether it is recognised. For example, items previously described as contingent liabilities that satisfy the definition of a liability would be recognised unless they cannot be measured reliably.

- specifies that a non-financial liability should be measured at the amount that an entity would rationally pay to settle the present obligation or to transfer it to a third party on the balance sheet date. Accordingly, the Exposure Draft explains that:
  - an expected cash flow approach is an appropriate basis for measuring a non-financial liability for both a class of similar obligations and a single obligation.
  - measuring a non-financial liability for a single obligation at its most likely outcome would not necessarily be consistent with the Exposure Draft's measurement requirement.
- specifies that a non-financial liability for a cost associated with a restructuring should be recognised only when the definition of a liability has been satisfied for that cost. Accordingly, a cost associated with a restructuring is recognised as a liability on the same basis as if that cost arose independently of a restructuring. Specific guidance for accounting for costs that are often associated with a restructuring is proposed as follows:
  - termination benefits to encourage employees to leave service voluntarily (voluntary termination benefits) should be recognised when employees accept the entity's offer of those benefits.
  - termination benefits provided as a result of an entity terminating employment (involuntary termination benefits) should be recognised when the entity has communicated its plan of termination to the affected employees and the plan meets specified criteria, unless the involuntary termination benefits are provided in exchange for employees' future services (ie in substance they are a 'stay bonus'). In such cases, the liability for those benefits should be recognised over the period of the future service.
  - a liability for costs that will continue to be incurred under a contract for its remaining term without economic benefit to the entity is recognised when the entity ceases using the right conveyed by the contract (in addition to any liability recognised if the contract was previously determined to be onerous). For example, the costs of an ongoing operating lease commitment on a property that is to be vacated is recognised when the entity ceases to use the leased property.
  - the cost of terminating a contract before the end of its term is recognised when the entity terminates the contract in accordance with the contract terms.

About the IASB

The International Accounting Standards Board (IASB), based in London, began operations in 2001. Contributions collected by its Trustees, the IASC Foundation, from the major accounting firms, private financial institutions and industrial companies throughout the world, central and development banks, and other international and professional organisations fund the operations of the IASB.

The 14 Board members (12 of whom are full-time) are drawn from nine countries and have wide international experience and a variety of functional backgrounds. The IASB is committed to developing, in the public interest, a single set of high quality, global accounting standards that require transparent and comparable information in general purpose financial statements. In pursuit of this objective, the IASB cooperates with national accounting standard-setters to achieve convergence in accounting standards around the world. Upon its inception the IASB adopted the body of International Accounting Standards (IASs) issued by its predecessor, the International Accounting Standards Committee (IASC). IASs 19 and 37 are two of the standards inherited from IASC.

A Deloitte & Touche study indicates that 94 countries either require or permit the use of IFRSs for publicly traded companies beginning in 2005. Some other jurisdictions, including Australia, New Zealand, the Philippines and Singapore, base their national practices on international standards. In September 2002 the IASB and the US standard-setter, the Financial Accounting Standards Board, reached an agreement to work towards the convergence of existing US and international practices and the joint development of future standards. In October 2004, the IASB and the Accounting Standards Board of Japan agreed to initiate discussions about a joint project to minimise differences between IFRSs and Japanese accounting standards towards a final goal of convergence of their standards. In January 2005 the two boards announced their agreement to launch a joint project to reduce differences between IFRSs and Japanese accounting standards, and in March the boards met to decide on the initial programme of work for the project.