



THE FINANCIAL REPORTING
REVIEW PANEL



2003

ANNUAL REVIEW

FINANCIAL REPORTING COUNCIL



The Financial Reporting Council's role is to promote good financial reporting and to act as the overarching and facilitating body for its two operational bodies, the ASB and the Review Panel.



The Accounting Standards Board makes, amends and withdraws accounting standards. It is assisted by its four committees—the Urgent Issues Task Force, the Financial Sector and Other Special Industries Committee, the Public Sector and Not-for-profit Committee and the Committee on Accounting for Smaller Entities.



The Financial Reporting Review Panel enquires into apparent departures from the accounting requirements of the Companies Act 1985 in the annual accounts of large companies and where necessary seeks remedial action, being empowered to apply to the court for that purpose.

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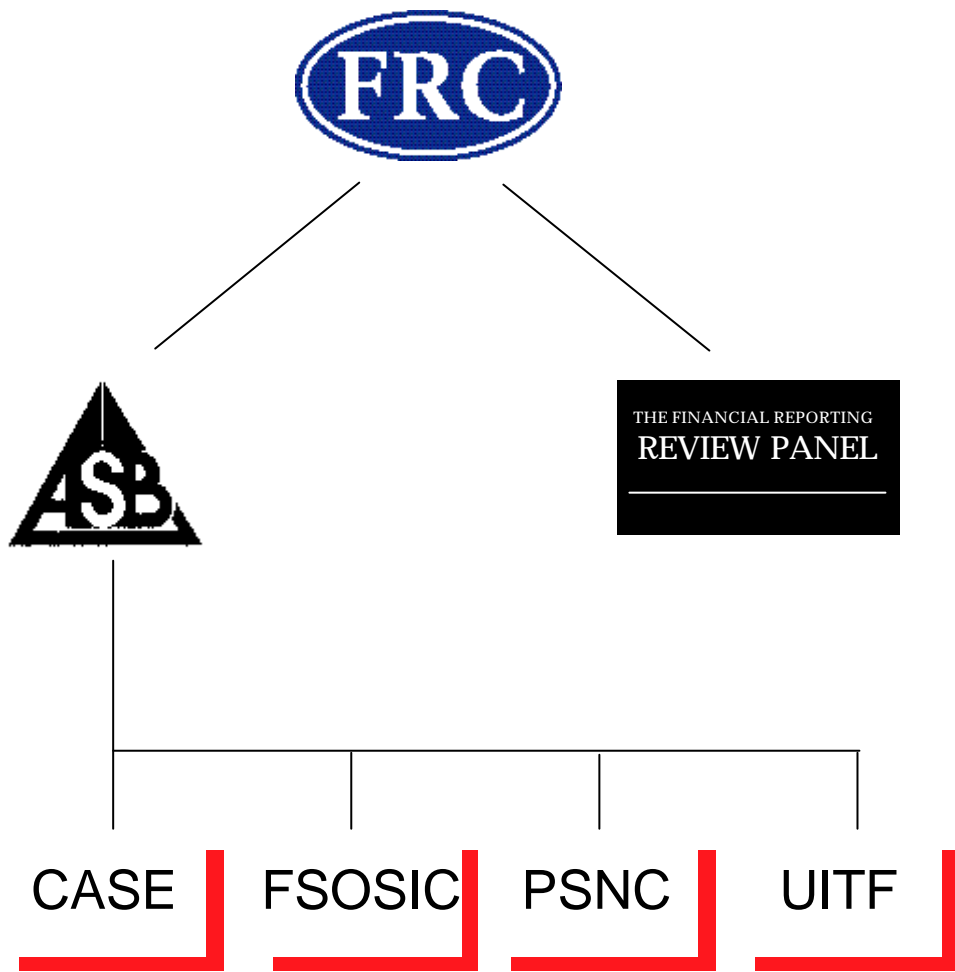
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CHAIRMAN'S REPORT

FINANCIAL REPORTING COUNCIL



CHAIRMAN'S REPORT

THE CHANGING REGULATORY FRAMEWORK FOR FINANCIAL REPORTING

1 This year has seen the FRC taking up a much enhanced role in the regulatory framework for financial reporting and corporate governance. This enhanced role builds on its existing responsibilities and comprises two main elements. The first is the increase in the level and intensity of activity in relation to the FRC's current remit and the second is to the assumption of significant additional responsibilities.

2 This enhanced role responds to the conclusions which the Government reached on the wide-ranging reviews of accountancy regulation and corporate governance in the UK. These reviews had been prompted by the collapses of Enron and WorldCom in the US. The reviews all recognised the importance of reassuring the markets and public at large that our financial reporting and corporate governance frameworks are sufficiently robust. Furthermore, in the context of global capital markets it was made clear that the ability to demonstrate the quality and independence of the regulatory regime is ever more important internationally. The regime is important in two ways. It contributes to the strength of London as a financial centre. Secondly, it helps to increase the ability of the UK to influence decisions which are important to it at home, but are increasingly being taken at international forums.

3 On 29 January 2003, the Secretary of State for Trade and Industry announced a package of reforms to raise standards of corporate governance, strengthen the accountancy and audit professions and provide for an independent system of regulation for those professions. The package included a number of recommendations that the Secretary of State looked to the FRC to take forward. The FRC was to give effect to the recommendations for improving corporate governance in the reports from Sir Derek Higgs and Sir Robert Smith (the Higgs and Smith reports). She said that the FRC would also assume the functions of the Accountancy Foundation (changed in certain important respects) so that, in addition to corporate governance, the FRC and its operating boards would then have three clear roles: -

- Setting accounting and auditing standards;
- Proactively enforcing and monitoring them;
- Overseeing the self-regulatory professional bodies.

4 With the assumption of these additional responsibilities, the FRC would become the new, single, independent regulator. The Secretary of State made clear that these recommendations were part of the package intended to "strengthen the foundations of our capital markets for the long term".

5 These measures, designed to effect a step change in the regulation of the financial reporting community, could have been taken forward by any one of a number of routes. It is, however, a tribute to what the FRC has achieved and what it represents that the Government wanted to put them in place by increasing the responsibilities of the FRC. The Government saw the FRC as a successful organisation with an excellent reputation. The Secretary of State also made clear that the new regime was to be "tough when that is needed, but measured and proportionate" and it is this that makes the FRC a particularly suitable organisation to take forward the Government's recommendations.

6 Essential to the FRC's success has been the support of the financial, business and professional communities at the most senior levels, demonstrating their commitment to high standards of financial reporting and corporate governance. The combination of Council oversight with the exercise on behalf of the Secretary of State of the relevant powers by the operational boards - the Accounting Standards Board (ASB) and the Financial Reporting Review Panel (FRRP) - has also allowed the regulation to be business-led, ensuring it was "light touch" and that due weight was given to its being cost-effective and proportionate. The FRC is now extending this approach to a wider remit. This takes in the setting and monitoring of auditing standards and the oversight of the accountancy profession, including investigation and discipline.

7 These new responsibilities are to be exercised alongside the FRC's existing responsibilities for corporate governance and accounting standards. It is being asked to enforce the latter proactively, an important change in approach for the FRRP.

8 All these developments can be seen as the sort of developments which the FRC has been ready to take forward over the years to respond to the changing needs of the financial and business communities. The Council last year supported those relevant to its existing remit - the introduction of proactivity and the work on corporate governance. This year, the Council at their May meeting accepted the new responsibilities for auditing and for overseeing the way the professional bodies regulate their members.

The FRC Responsibilities

9 The FRC will maintain its current responsibilities for the work of the ASB and the Panel. Developments in these areas are discussed briefly in my report at paragraphs 38 to 57 and in the separate chapters by the chairmen of each organisation. In addition, the FRC will include three other boards under its umbrella to meet its extended additional responsibilities. First, there is a new board, the Professional Oversight Board for Accountancy (POBA), and then there are two existing boards from the Accountancy Foundation, the Auditing Practices Board (APB) and the Accountancy Investigation and Discipline Board (AIDB).

10 Sir John Bourn has agreed to chair the new POBA. This has three main roles. First, the Government plans to bring forward legislation to delegate to it the statutory functions the Secretary of State for Trade and Industry currently exercises in relation to audit by authorising the professional accountancy bodies to act as supervisory bodies and to offer a recognised professional qualification. Secondly, it will establish and oversee an independent Audit Inspection Unit to monitor the audit of major listed companies and other public interest entities, including both the audit process and the decisions taken by the auditors. Thirdly, it will oversee the regulatory activities of the individual professional accountancy bodies, including education and training, standards, professional conduct and discipline.

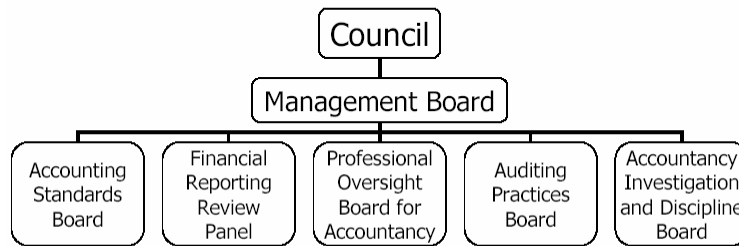
11 The second board, the APB, is chaired by Richard Fleck. It plays a key part in the development of auditing and assurance services standards and their effective application. Its responsibilities have also been extended to the development of ethical standards relating to the independence, objectivity and integrity of auditors. It has recently published a consultation document on this subject. As in the case of the ASB, there is a strong growing international dimension to this work.

12 The third board is the AIDB chaired by Mike Fogden. An effective and transparent investigation and disciplinary scheme to handle public interest cases will be an important part of the new arrangements. Preparatory work was done under the auspices of the Accountancy Foundation, but the Government has made it clear that early introduction of the scheme should be one of the new FRC's priorities.

13 The organogram below shows these five boards, together with the Council and with a new feature, the Management Board. The Management Board is the most visible sign of the changes which will take place in the organisation with its new, broader span of responsibilities. Hitherto, the FRC has been able to exercise its strategic oversight and its

management responsibilities for the ASB and the FRRP with minimal formal structure and resource. The new much larger organisation with the responsibility of delegated statutory powers, will require a more formal structure. The Management Board has been set up to see that the FRC's responsibilities are properly exercised and demonstrate the unity appropriate to the FRC's status as the single, independent regulator. It will comprise the five chairmen of the subsidiary boards and the FRC directors - myself in the chair and the chief executive. In addition, with the greatly increased range of responsibilities, the Council will meet four times a year rather than two as at present. A strengthened secretariat is being put in place to provide the necessary support for the larger organisation.

NEW FRC



14 In addition to these organisational changes, the membership of the Council itself also needs to change in order that it can best meet its new, enhanced role. Proposals for these changes were put to the Council, together with the organisational changes outlined above. The Council endorsed both at its meetings in May and July. They will require changes in the constitution of the FRC which are under way.

15 The changes outlined above reflect the importance of demonstrating an appropriate degree of accountability and transparency in the new context. To explain those changes further they need to be reflected in the composition both of the Council and in the criteria for appointment as FRC chairman and deputy chairmen and directors. On the Council, it was agreed that the FRC should continue to be a "big tent" organisation, but that the spread of representation needs to change within the overall membership number of thirty. The Council needs to accommodate three additional board chairmen. It must also demonstrate suitable independence from the accountancy profession. The Council recognised that the chairman, deputy chairmen and directors should strike the right balance between independence and the legitimate interests of key

stakeholders. The FRC proposes to meet these conflicting demands through a board of directors consisting of an independent chairman and deputy chairman and three directors, representing the key stakeholder interests of business, the accountancy profession and the investor community. These appointments will be made by the Secretary of State for Trade and Industry following an open recruitment process for the chair, and deputy chair posts and following recommendations from the relevant constituencies for directors. All other appointments within the system will be made by the board of directors after following procedures and consultation processes in line with best practice.

16 The Council has agreed the main points for the constitution and the organisation. Our lawyers are now working on the formalities of putting the new FRC constitution in place with changes in the FRC's Memorandum and Articles to reflect the proposals the Council has endorsed. The formalities of the FRC's relationship with the boards will be modelled on those of the existing FRC subsidiaries. These changes will also be designed to achieve the greater transparency and accountability that the FRC recognise is particularly important in the new context.

17 We have published on our website aims and objectives for the FRC and all its boards. Each board has published a high level work plan.

18 In developing the constitution and the organisation to meet its new responsibilities, the challenge is to maintain the broad approach to regulation which has served the FRC well, and which has been emulated elsewhere, while putting in place arrangements which can best meet the needs of the new environment and, at the same time, are transparent and provide proper accountability.

Financial Implications and Funding

19 Our present funding arrangement, with support coming in equal shares from the Government, business and the accountancy profession, is a further element that has been important to the success of the FRC. It guarantees the independence of the organisation since no single interest group dominates. It reflects the public interest in good financial reporting and the principle that the business, financial and accounting community should provide tangible support for these activities, recognising that they benefit from them. The Council endorsed this approach at their July meeting. The Government has already indicated its own commitment to continuing this arrangement, as has the accountancy profession. Discussions with representative business organisations show broad support for maintaining the principle. I have now written to the chairmen of all listed companies seeking their agreement to an increase in the levy to fund the business share of our costs.

20 Inevitably, the new regulatory regime, with its higher level of activity, will cost more. The FRC and the Accountancy Foundation each presently costs £2.6m for the current year. The costs of a more proactive regime for enforcing accounting standards could rise over the next three years or so from its present level of £0.3m to some £3m. The costs for the FRC itself will inevitably rise if it is to provide effective oversight of its much wider range of responsibilities and an appropriate level of accountability. In broad terms, over the next three years our budget requirements to be in the region of £12m. In addition, firms will meet the costs of audit monitoring through fees as they do now, and the costs of cases going before the Investigation and Discipline Board will be met, as now, by the profession. Although the increase is significant, the absolute costs are relatively modest given the weight and importance of the task of strengthening the regulatory framework and the benefit of its contribution to business and market confidence. If it is to be done well, it must involve appropriately paid high calibre people.

Practical progress towards establishing the new unified regulator

21 The Council's endorsement of the recommendation that the FRC should become the new, single, independent regulator for accounting and auditing, and that it should take a more proactive approach to the enforcement of accounting standards and be more active in its corporate governance role, are important milestones. At the same time much progress has been made to enable the FRC to start operating as the new single regulator.

22 Our priority has been to be operationally unified in practical terms as soon as possible, with the legal formalities to follow. I have had regular meetings with all the chairmen throughout the year and collective formal meetings - now the Management Board - since April. There is a significant body of work required to set up the new legal constitutional arrangements and we are working with the Government to ensure that the FRC arrangements fit sensibly with the planned legislative framework. Work on budgets and funding is well advanced so that we will be able to operate from a single budget at the start of our financial year 2004-2005. Appointments to the key posts in the new organisation are expected to be made by the end of the year. There are a number of additional practical issues to be tackled for the organisation to operate fully as an effective, single unit. These include rationalising contracts, terms of employment, suppliers and so on but the most difficult of all these is the question of premises, where there are real problems in achieving the objective of bringing everyone together on a single site as soon as possible.

23 The determination of the Government that their package of measures to strengthen the financial reporting and corporate governance framework must be implemented as quickly as possible has been a critical factor in enabling such rapid progress to be made. The DTI set up an implementation steering group chaired by the Government representative on the FRC, Stephen Haddrill, and whose members included myself for the FRC and the outgoing Accountancy Foundation, and Peter Wyman, a former FRC deputy chairman and CCAB chairman, for the CCAB. This provided an important mechanism for overseeing the process of operating as the "new" FRC and resolving issues as they arose. This mechanism was, I believe, also helpful in developing an approach to interim funding for the organisation, and I would like to record appreciation for the constructive and helpful approach the Government has taken to this essential practical matter. The DTI implementation steering group was backed up by an internal FRC progress group chaired by myself.

24 The Government has now brought forward their legislative proposals for this area in the Companies Audit, Investigations and Communities Enterprise Bill. These proposals would require the professional accountancy bodies that supervise auditors to sign up to independent standard-setting, monitoring and disciplinary processes. The government expects that they will fulfil these requirements: by ensuring that their members follow technical and independent auditing standards set by the Auditing Practices Board (APB); to by submitting to monitoring by the Audit Inspection Unit in respect of the audits of listed and other large companies; and by complying with investigation and disciplinary proceedings under the auspices of the Accountancy Investigations and Discipline board. The legislation would provide a power for the Secretary of State to delegate her functions under Part II of the Companies Act 1989 (essentially, the recognition of supervisory bodies and qualifications for auditors) to a body - the intention being be delegate them to the POBA. The Government are also intending to create a gateway for the Inland Revenue to pass information to the Panel, thus providing a new source of information to the Panel. In addition, the Government is considering using their existing powers to implement the proposal for a statutory Operating and Financial Review (OFR) for large companies. The FRC noted at its July meeting that the Government remain committed to the programme of comprehensive company law reform, to which the FRC has contributed both as an organisation and through individual members. They plan to legislate as soon as is consistent with ensuring that the extensive changes required would be clear, coherent, deliver for business and would stand the test of time.

THE COUNCIL

25 At the same time as contributing to these developments, the Council, the ASB and the Panel have continued their normal day-to-day work. For all three bodies, the international dimension continues to increase in importance. Our regime needs to be well understood internationally for two reasons. Firstly to inform those with a potential interest in London as a financial centre, and secondly because developments in the EU and in the US increasingly impact on operations here. I have, therefore, met leading members of the European Commission and in the US of the Congress, the Securities and Exchange Commission, the Public Company Accounting Oversight Board (PCAOB) and others to explain to them the new role of the FRC and the developments here in financial reporting and corporate governance. This has also been important to the ASB and the Panel, as the reports from their chairmen clearly show.

26 Relatively few changes took place in the membership of the two operational bodies themselves: there were three new appointments to the ASB including a new Technical Director and one Panel member whose term of appointment ended. At the ASB, the most significant change will take place when Allan Cook steps down as Technical Director at the end of the year. His contribution is discussed later in this report. Appointments to these two bodies are the responsibility of the Appointments Committee, whose members are identified in Appendix 1. I am grateful to the Committee for their work reviewing and renewing appointments so that the membership of the bodies is appropriate for the work of the Board and the Panel.

27 On the Council itself, the term of office of the Deputy Chairman, Peter Wyman, came to an end. I thank him for his contribution. Three other Council members completed their periods of service: David Challen, David Bishop and Hilary Cropper. We appreciate the contribution they made. David Illingworth, now the Chairman of the Consultative Committee of Accountancy Bodies, succeeded Peter Wyman as Deputy Chairman.

28 It is with great pleasure that I mention that three members of the organisation were granted honours during the year. Sir David Clementi and Sir Derek Higgs, both Council members, were knighted, and Ann Wilks, Secretary to the Council, was appointed CBE.

29 A full list of the current membership of the Council is in Appendix 1.

CORPORATE GOVERNANCE

The Higgs and Smith Reports and the Combined Code

30 In January Sir Derek Higgs published his report 'Review of the role and effectiveness of non-executive directors' (the Higgs report), undertaken at the request of the Government ; and on the same day the FRC published the report of the group set up by the FRC and chaired by Sir Robert Smith 'Audit Committees: Combined Code Guidance' (the Smith report).

31 Both had received broad support on publication. But certain aspects of the Higgs report thereafter became more controversial. The Higgs report argued persuasively for its recommendations to strengthen the role of non-executive directors and the transparency and accountability of boards to shareholders. The Smith report was equally persuasive on the need for strengthening the role of the audit committee, particularly in overseeing the integrity of the company's financial statements and in reinforcing the independence of the auditors.

32 The Higgs report included a suggested revised Combined Code, reflecting the recommendations of his own report and the Smith report. It fell to the FRC, as guardian of the Code, to take up this suggestion and I announced a 12-week public consultation on his draft.

33 There followed a lively debate: more than 180 responses to the consultation were received, alongside a good deal of discussion in the press and elsewhere. It emerged that many commentators were broadly content with the recommendations in the main part of the Higgs report but had misgivings and objections about how some of these had been carried over to the suggested Code. It became clear that some substantive changes and some significant redrafting would be needed in order to achieve the degree of broad consensus necessary for the successful launch of a revised Code.

34 I read all the responses and consulted with the representative bodies and interested individuals, and from this process a constructive way forward emerged. I met with a group of Council members to decide on proposals for some substantive changes to the proposed Code and for an approach to redrafting to be put to the Council's May meeting.

35 The May Council meeting endorsed these changes and approach and set up a working group under my chairmanship to produce a redrafted version of the Code to be put to special meeting of the Council in July. The membership of the working group is shown in (Appendix 1). I am extremely grateful to the members of the group for their positive and constructive approach.

36 The group worked intensively on the draft from May to July, consulting the main representative bodies closely. Throughout, we had in mind the need for a high-quality Code but also the need for it to command broad support from all sides of the business community, without which it would have no credibility.

37 At the July Council meeting we agreed the final text of the new Code, which we published immediately. It came into effect from 1 November. It incorporates the main substance of, and most but not all, the recommendations in both reports. I believe it will foster far-reaching changes in British boardroom practice and its provisions for rigorous selection, professional development and performance evaluation will help to develop further the professionalism of non-executive directors.

38 There remains a concern about communication between company boards and institutional investors on Code issues. There needs to be mutual trust and understanding based on regular constructive dialogue. Both sides need to work hard at this. It is particularly important to the working of the widely supported comply or explain principle. It is expected that most companies will comply most of the time. However there will be occasions when companies for one reason or another judge that non-compliance is appropriate in a particular case. When this happens, companies need to make the effort to ensure that shareholders fully understand the reasons for the departure from the Code. Equally, shareholders need to ensure that they listen to the company's explanations - even if in the end they remain unconvinced and vote against as they are of course entitled to do.

39 When the Higgs report was published, the Government asked Laura Tyson, Dean of London Business School, to consider how to improve the recruitment and development of non-executive directors. One conclusion on training opportunities for non-executive directors was that there were possible gaps between what training providers currently offer in this area and what companies need. The Tyson group recommended that "an organisation such as the Financial Reporting Council or the London Stock Exchange convene a group of providers and companies to establish guidelines to ensure that practical board training programmes for directors provide what is needed." We are pursuing this in conjunction with others knowledgeable in this field.

ACCOUNTING STANDARDS BOARD

40 At the ASB, there have been three departures - David Allvey, John Coombe and, at the end of the year, Ken Wild. All have contributed significantly to the work of the Board. Jon Symonds joined the Board in September and Mike Ashley will be joining on 1 January, as will Andrew Lennard as the Board's new Technical Director. Details of membership are in Appendix 1.

41 The most significant change for the ASB is that Allan Cook steps down as Technical Director at the end of the year, though he will continue to work with the ASB. Allan has been Technical Director since the ASB was established. The great respect in which the ASB is held both internationally and in the UK owes much to his technical mastery and his dedication. Mary Keegan pays tribute to his work in her report. I record the appreciation and gratitude of the Council for his contribution over more than thirteen years.

42 As Mary Keegan's report shows, it has been another extremely busy year for the ASB and its staff. It has also been in some ways a frustrating year. The dominant objective has been to ensure that the International Accounting Standards Board (IASB) puts in place a comprehensive set of high-quality standards; and that the European Union adopts those standards in their entirety in time for 1 January 2005. Progress depends on many factors over which we have no control, and it has not been as rapid or as smooth as the ASB would have wished.

43 The IASB has an enormous task and is pursuing it vigorously. It was of course not the IASB, but European Ministers, that set the January 2005 date for bringing the EU Regulation on international accounting standards into effect. Perhaps those concerned did not fully appreciate the amount of work that had to be done by the international standard-setting community in turning the standards the IASB inherited when they came into being in 2001 into the comprehensive, modern and robust set of standards that Europe needs.

44 In December, the IASB completed its 'Improvements' project and issued fifteen revised standards in final form. We expect soon to see new standards on controversial topics such as share-based payment and business combinations. But gaps remain, for example in insurance accounting; and a key joint IASB/ASB project on 'Reporting Comprehensive Income' needs to regain momentum.

45 This is frustrating for the ASB. Delays have made it impossible to achieve, as intended, the phased introduction of new UK standards based on IASB material in the run-up to 2005. More importantly, there is a real danger that from a technical point of view the overall standard of financial reporting in the UK will not improve from January 2005 and may even in some respects fall.

46 There is also some cause for concern about the EU process of adoption, as Mary Keegan's report explains. It is essential that the EU adopts the complete set of international standards and does not pick and choose. There will almost always be some interest group that dislikes a particular proposal, certainly in the controversial areas such as accounting for financial instruments, share-based payment and pensions. If the principle of a comprehensive move to international standards is breached in one area, pressure for further breaches will become irresistible. I hope that the Commission understands this and will avoid falling into the trap. But I share ASB concern that the exclusion of two international standards from the EU adoption decision of September is not a good precedent.

47 The ASB can only exert an influence on these developments by constant interaction with its counterparts in Europe and around the world, and with the IASB itself. This is extremely time-consuming for Mary Keegan herself and her staff but it is an essential part of the job. So too is constant contact with interested groups in the UK. A great deal of time and effort is rightly devoted to this and Mary Keegan is able to speak with all the more authority in the international arena as a result.

48 For the future, the ASB's domestic responsibilities depend very much on the Government's decision on the options to extend the application of the EU Regulation beyond the consolidated financial statements of listed companies. The Department of Trade and Industry announced in July that use of international accounts would not be mandatory for any other financial statements but would be permitted for all. The need for UK standards will therefore remain for those companies and other reporting entities that opt to continue using them. The ASB intends to bring UK standards into close convergence with international standards, over a timescale to be determined, as Mary Keegan's report explains. There will also need to be a very careful consideration of the SORP regime.

49 The ASB continues doing other useful and important work focusing on financial reporting needs within the UK. Three examples demonstrate this: the Operating and Financial Review, an updated version of which the ASB published at the beginning of the year - we await further news of the Government's plan for a mandatory OFR; the Proposed Interpretation for

Public Benefit Entities of the Statement of Principles for Financial Reporting - an exercise in interpreting a statement of principles designed primarily for profit-oriented entities for quite different institutions such as charities; and the Application Note on Revenue Recognition, published in November, which spells out best practice in this fundamental but difficult area.

50 These brief highlights, and much more so the ASB chairman's report, show that the demands on the ASB in this transitional period are challenging in terms of both the nature and scale of the issues to be addressed. The international environment further complicates matters. The Council provides both broad support and sufficient resource for the work of the ASB and remains an important source of strength.

FINANCIAL REPORTING REVIEW PANEL

51 First, on the Panel itself, the only change this year has been that David Mitchell, a founder member, stepped down. We appreciate his long service.

52 This year, there have been three important aspects to the Panel's work. Firstly, following the Government recommendation that accounting standards should be proactively enforced, the Panel has developed its approach, made a start on its new role and agreed its working relationship with the FSA. Secondly, it has become more actively involved in developments on enforcement in the EU. Finally, its normal caseload has continued. In his report, Richard Sykes discusses these areas in more detail. I comment here from the Council's perspective.

53 As the Panel develops its proactive approach, the Council will be keen to ensure that this is done in a way which strengthens the regulatory framework as a whole. An element in the success of the Panel to date is that it has reinforced the commitment to high standards of financial reporting among those whose frontline responsibility it is, namely the Board of Directors and the auditors. There is always a risk that a higher level of activity on the part of the regulator will be seen as a shift of responsibility in that direction. If Panel proactivity is to increase the effectiveness of financial reporting regulation as a whole, however, it needs to be a way of strengthening the support for those actively involved elsewhere.

54 Developing an approach to the proactive review of financial information which is cost-effective has been one of the most difficult challenges in implementing the Government recommendations. It is accepted that reviewing all listed companies on the UK regulated market could not be justified in terms of cost. Determining criteria for deciding how many companies, selected by what criteria, should be reviewed is a difficult question to answer. The Panel is adopting an approach which takes account of the probability of mis-statement occurring and the potential impact of any such mis-statement on market and investor confidence. Factors such as governance, reputation, comprehensibility and disclosure will also be important signposts. The selection process will be dynamic and will change as issues emerge and the economic and financial environment changes. In arriving at the detailed criteria, the Panel will consult a representative stakeholder group being set up under FRC auspices to identify areas of contemporary risk in relation to industries and sectors. However carefully this work is done, the Council agrees with the points frequently made by the Panel that its activities must not be seen as guarantees of the accuracy of the financial statements which no regulatory system can ever provide.

55 The Panel has long recognised that it must have appropriate contacts with other regulators who have a role in the financial reporting framework. For some years now, there has been liaison between the Panel and the professional bodies to ensure that they are aware of Panel findings involving their members. Of specific interest in the context of proactivity, however, is the way in which the Panel and the FSA will be working together.

56 In the particular context of proactivity, the Government endorsed the recommendation that there should be a closer working relationship between the Panel and the FSA, a relationship to be defined in the Memorandum of Understanding. The Panel and the FSA have agreed on their respective roles, and agreed a Memorandum of Understanding. Responsibility for proactivity, including the selection of accounts, will rest entirely with the Panel. The FSA will, though, provide the Panel on a regular basis with information which, in their opinion, will be of interest to the Panel.

57 The importance of working with other regulators was further underlined in another recommendation, namely that a gateway should be created to allow the Inland Revenue to pass to the Panel any information about company accounts which they uncovered in the course of their tax work and which could be of interest to the Panel in their role as the enforcers of accounting requirements. At present, the law prevents the Revenue from doing so. The Government's legislative proposals would enable this to happen.

58 As at the FRC itself, and still more so at the ASB, the Panel activities are now also being shaped by developments in the EU. The Commission is keen to develop a co-ordinated approach to the enforcement of accounting standards. It has looked to securities regulators, who commonly have a responsibility for accounting in EU member states, to develop this. The FSA are involving the Panel in this work. The Council very much welcomes the fact that the expertise which the Panel has is thus being made available more widely in the EU, and that it may contribute to any future regime better serving the needs of the UK financial and business community.

59 In the context of both proactivity and prospective EU developments, further thought is being given to what might be the most appropriate legal framework to enable the Panel most effectively to exercise its new responsibilities.

60 As these developments proceed, the Council will aim to see that those characteristics that have made the Panel successful are maintained. These include the standing and reputation of the Panel, the involvement of respected experts and the avoidance of a formulaic approach to cases. The Panel approach enables questions of judgment to be considered. The results of these debates, whether in a Panel finding or in other ways, make a real contribution to better financial reporting. The Council will look for reassurance that this element of the Panel's work can continue in its changing operating environment.

FINANCE

61 The FRC's financial year runs to 31 March and details of its financial affairs to March 2003 were set out in its report and financial statements published in June. A summary of the main figures is given in Appendix 2.

62 As set out in Appendix 2 the total operating charges of £2.8 million in the year to 31 March 2003 were the same as those of the previous year (£2.8 million). It is likely that operating expenditure in this current financial year net of income will remain consistent with the last year. However, planned increases will arise due to the introduction of greater Panel proactivity and the incorporation of the activities of the Accountancy Foundation. In the present financial year, these are being met either by the Government as the cost of implementing their recommendations or by the CCAB as part of the budgeted support they had agreed for the Accountancy Foundation functions.

63 The willingness of the financial business and professional community, together with government, to meet our costs have been essential to the success of the arrangements. Their contributions provide a tangible demonstration of the support we draw from a wide range of constituencies. Most important however has been the commitment to ensuring that the operation is adequately funded particularly at a time when it is facing increasingly heavy demands on its relatively modest resources. On behalf of the Council, I should like to express our thanks to all the contributors for their vital part in our success.

CONCLUSION

64 This year will be the last time that the FRC publishes its Annual Review in its present form. Next year's Review will cover the activities of all the Boards that will be part of the FRC. The next review will show how all responsibilities that will fall to the FRC have come together creating a single independent regulator.

65 It will be clear from my report that making progress towards this outcome is one of two areas that have dominated the work of the FRC. The second is the work the Council took on to translate the recommendations in the Higgs and Smith reports into a Combined Code that commanded broad consensus and support.

66 These two areas raised very different and often difficult issues. Challenging issues of this kind do and will certainly continue to arise. The outcome is much improved by working with all our stakeholders. It remains as important as it has been hitherto to consult with and listen to them. But ultimately it is with the directors and the Council that responsibility lies. In making and in taking forward decisions within our extended area of responsibility, their judgement and support will be critical to the continuing success of the FRC. The views of the Council will help to win acceptance for policies which aim to meet the best interests of the financial reporting community but which may not be popular in the short term especially with some groups of stakeholders.

67 The willingness of our stakeholders and of the Council to play their full part in the process is vital to its success. This requires time and effort on their part. I very much appreciate and am grateful for the important contribution they make in doing so.

68 In focusing on the changes for the FRC, it is important not to lose sight of what has been achieved during the year in their continuing areas

of responsibility. For the ASB, their task in maintaining and improving the highest standards of financial reporting becomes ever more complex and difficult-both on account of the nature of the issues and the international environment in which it has to operate. Mary Keegan's report makes this clear. I recognise that the ASB continues effectively to influence the outcome through the quality of its contribution. Mary Keegan's vision and leadership together with the contribution of her colleagues on the board have been vital to this. We are grateful to them.

69 This year, the Panel has again had to take forward work on proactivity and to contribute to European developments as well as handling the cases in the normal way. I should like to thank all Panel members and particularly the chairman, Richard Sykes and the deputy chairman, Ian Brindle for the progress that has been made in these different areas.

70 Finally, the effectiveness of the FRC the ASB and the Panel depends very much on the staff who work for them , whether they are directly employed or on secondment. In the past year, the work of each of the bodies has continued to place very heavy demands on the staff. I would here like to record the Council's thanks to all of them. They are listed in Appendix 6.

71 In addition, I would like to record our immense gratitude to Ann Wilks, who as Secretary to the FRC has worked tirelessly and effectively to ensure the new organisation goes forward in good order. Ann has delayed her planned retirement this year to remain with us until the new Chief Executive takes up post in 2004. Throughout her time at the FRC she has given us the benefit of her wide experience of Government and excellent judgement and leadership ability, all of which have proved to be invaluable over the past months of intense change. Her energy and determination have enabled her to handle a prodigious personal workload successfully and to motivate and lead others to do the same. I am particularly appreciative of the sterling support she has given me personally in carrying out my functions as Chairman. We wish Ann a long and happy retirement.

BRYAN NICHOLSON



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CHAIRMAN'S REPORT

ACCOUNTING STANDARDS BOARD

CHAIRMAN'S REPORT

INTRODUCTION

1 Listed companies in the UK and the Republic of Ireland, many of which trade, invest and seek capital in international markets, have benefited considerably from the strong reputation which UK accounting standards presently enjoy across the world. From 2005 these companies must, in place of UK standards, use European Union adopted international accounting standards (adopted IFRS) to prepare their group financial statements.

2 The UK and the Republic of Ireland have a considerable interest in seeking to ensure that the move to adopted IFRS does not - either in fact or in perception - result in a reduction in the quality of financial reporting. If this is to be achieved, it is essential that by the end of 2004 a set of high-quality standards is issued by the International Accounting Standards Board (IASB) and adopted by the European Union (EU).

3 With this deadline fast approaching, the work of the Accounting Standards Board has in 2003 focused particularly on the international agenda. We have continued to work directly with the IASB and have sought to influence its projects to improve and extend existing international standards. We have published and explained the international proposals for our constituents in the UK and Ireland and encouraged them to make their views known to the IASB. We have also participated in extensive discussions with standard-setting colleagues across the world and with those who will be influential in the EU adoption process.

4 At the same time, we have not neglected the domestic agenda. This year the Board has issued a revised Statement on the Operating and Financial Review and an accounting standard on Revenue Recognition. The Urgent Issues Task Force (UITF) has issued new Abstracts on sales of capacity and on purchases and sales of own shares, as well as consequential revisions to Abstracts on Employee Share Ownership Plans.

5 The Board has also issued a consultation document on the interpretation for the 'public benefit' sector of its Statement of Principles for Financial Reporting, and has continued its work with the industry bodies that issue Statements of Recommended Practice (SORPs). A list of 2003 publications is given in Appendix 3.

6 In both our domestic and international activities, we continue to benefit greatly from consultation with UK and Irish constituents. This is a time-consuming but essential part of our work - not just due-process consultation on exposure drafts but also regular meetings with interested groups. We aim to ensure that both our pronouncements and those of the IASB respond in a balanced way to constituents' legitimate concerns.

7 We have good links with the bodies which comprise the Institutional Shareholders Committee (representing users of financial statements), with the Hundred Group of Finance Directors, the Quoted Companies' Alliance and the CBI, and with industry bodies such as those representing retail and investment bankers, insurers, treasurers and the property and leasing industries. We also meet regularly with representatives of the accountancy professional bodies and the ten largest firms of accountants, with leading academics and with the Financial Services Authority (FSA).

8 These meetings are important in stimulating debate on financial reporting; they also have an important educational focus in the transition to international standards. ASB staff has continued to take advantage of a wide variety of opportunities to speak at conferences, in order to explain to the UK and Irish constituencies the forthcoming changes in financial reporting. We were also pleased that our website (www.asb.org.uk), which includes both project reports and our quarterly newsletter Inside Track, won press recognition this year for its clarity and content.

INTERNATIONAL STANDARD-SETTING

9 The IASB has continued to make good progress during 2003 but has fallen somewhat behind its original ambitious timetable. When it started its work in 2001, it inherited a substantial number of standards from its predecessor body; significant work was needed to make these suitable for introduction as required standards in Europe and elsewhere. It also identified a number of projects requiring radically new thinking on financial reporting (notably accounting for insurance contracts, share-based payment, off balance sheet finance such as leasing and the reporting of financial performance).

10 When Europe's Ministers decided that the EU should move to international standards, they chose the early date of 2005, perhaps not fully appreciating the magnitude of the IASB's task. In consequence, and perhaps not surprisingly, a number of development projects on the IASB agenda which we had considered of importance in UK reporting have had to be delayed.

11 The IASB has now undertaken that all new and revised standards coming into mandatory effect in 2005 will be issued in final form no later than March 2004. For the rest of 2004 it proposes a 'period of calm'. This seems a sensible decision and one which should allow the EU's adoption processes time to agree the standards; it does however add to the present time pressure. It is possible that the IASB will issue further standards for voluntary adoption from 2005 but these will not be mandated before 2006.

12 Overall the standards available for EU adoption for 2005 seem likely to include only two substantive new areas of accounting as far as the UK and Ireland are concerned: 'mark to market' reporting of derivatives and other financial instruments, and the expensing of share-based payments. Use of adopted IFRS will, however, also bring changes in many other areas of financial reporting and not least as a result of the IASB's programme to bring about convergence of its standards with those of the USA, announced in September 2002.

13 Appendix 4 sets out our current understanding of the progress towards the 2005 adopted international standards, though it is of course somewhat dangerous to forecast the work of another standard-setting body!

14 Twelve of the IASB's inherited standards will remain unchanged; these have already been adopted by the EU process and are therefore ready for use at 2005. A new standard on the first time adoption of IFRS was issued in June 2003. Fifteen 'improved' standards, including two on financial instruments, were issued in December.

15 The remaining standards due before the IASB's March deadline are:

- on share-based payment (originally planned for implementation in 2004 - now to be 2005);
- on business combinations, with related amendments to standards on impairment and intangibles;
- on discontinued operations;
- interim guidance on insurance contracts; and
- limited amendments to the standard on measurement and recognition of financial instruments, dealing with hedge accounting.

It is notable that the standards on insurance contracts and business combinations are interim measures; it will not be until well into the second half of the decade that we can expect comprehensive international standards on these subjects.

16 Not presently clear on the IASB's publications agenda, but important for the UK and Ireland, is its work to amend the international standard IAS 19 'Employee Benefits', announced in July 2002. Decisions since taken at IASB meetings lead us to believe that the international board may favour the immediate recognition of pension surpluses and deficits (as required in the UK's FRS 17). This is currently available under adopted IFRS; however the existing international standard does not permit segregation of the effects of actuarial gains and losses in the Statement of Recognised Gains and Losses. At its meeting in December 2003, the IASB tentatively agreed to issue an exposure draft of limited amendments to IAS 19 to facilitate accounting as in FRS 17. We hope that time will permit the finalisation and EU adoption of such amendments to make them available for use by UK and Irish companies in 2005.

17 We have maintained our usual close contacts with the IASB throughout this year. Geoff Whittington, the IASB liaison member for the UK, attends our Board meetings and receives briefings from ASB staff before the international meetings. In addition to our participation in the IASB's regular meetings with its 'partner' national standard-setters, we have frequent informal contact with the IASB at all levels. We have written formally to the IASB on all its proposals.

18 We have also used, wherever possible, a further channel of comment available to us through the Technical Expert Group of the European Financial Reporting Advisory Group (EFRAG), of which Allan Cook is a member. The Technical Expert Group's formal objective is to give advice to the European Commission on the adoption of the IASB's standards for use in Europe. It has also taken the view that it should comment to the IASB on its exposure drafts; it stimulates a debate across the EU by publishing early drafts of its responses to the IASB and inviting comments. The ASB has provided detailed comments to EFRAG on these draft responses. We have also sought to use EFRAG's periodic meetings with Europe's national standard-setters to listen to views from other member states.

EUROPEAN DEVELOPMENTS

19 The delays and uncertainties surrounding the IASB's programme have been somewhat compounded this year by concerns about the European process for adopting the IASB's standards.

20 It is the responsibility of the European Commission to make proposals for the adoption of the IASB's standards to the Accounting Regulatory Committee (ARC) of member states' representatives. The

Department of Trade and Industry (DTI) represents the UK in this committee; the Republic of Ireland is represented by its Department of Enterprise, Trade and Employment. The ARC has 'comitology' powers (permitting a significant shortening of the normal EU law making process) and makes decisions by qualified majority voting.

21 In the spring of 2003 the Commission proposed the adoption by the ARC of the standards inherited by the IASB in 2001, but with the notable exception of IASs 32 and 39. IASs 32 and 39 deal with the recognition, measurement, presentation and disclosure of financial instruments and pre-date the EU's decision to use international standards. This first round of the adoption process went to a formal vote in July and was completed in September; it included many standards, including those in course of amendment under the 'improvement' and business combination projects. There will thus need to be several further adoption processes before 2005 once the standards are in final form, if Europe is to apply a modern set of standards.

22 IASs 32 and 39 have been the subject of particular controversy and vigorous lobbying by business in some EU member states. Most notably, there have been - and continue to be - considerable efforts to resist IAS 39's requirement for derivatives and other financial instruments to be 'marked to market' and the restrictions which the standard imposes on the deferral of the resulting gains and losses (the 'hedge accounting restrictions'). Most people understood that the financial instrument standards needed revision before 2005 to assist in implementation and the IASB had, by the spring of 2003, already put forward amendment proposals and started a process of dialogue with the banking community. It seemed odd, however, that the European Commission should propose the adoption of a number of standards that were in process of amendment, but not those on financial instruments.

23 In July, EU Finance Ministers became engaged in the debate, following an intervention from the President of France questioning the effect of the IASB's standards on financial instruments in the European environment. We were pleased that Finance Ministers, whilst encouraging the IASB to continue its dialogue with European industries most affected, underlined the importance of EU adoption of IASs 32 and 39.

24 Nevertheless, the selective approach taken by the European Commission this year suggests that we cannot be certain of the European outcome. The UK Board has always seen the move to IASB standards as a positive step towards its goal of global standards even if, on occasion, this requires the acceptance of some standards with which we are not wholly content. We are anxious to see the full set of '2005 standards' adopted in Europe as soon as possible.

25 Furthermore if, after March 2004, the IASB issues further new standards, we will be keen to see these adopted by the ARC on a timely basis, to allow their early use by UK and Irish companies. This may be attractive, for example, to avoid successive changes in accounting policy in respect of the same item; however, it will only be available to EU companies if the adoption process works expeditiously.

26 We are particularly concerned to see the adoption of IASs 32 and 39, albeit in their amended form. The absence of these standards from those to be applied in 2005 would leave companies with no international equivalents to FRS 4 'Capital Instruments', FRS 5 'Reporting the Substance of Transactions' and FRS 13 'Derivatives and other Financial Instruments: Disclosures'. This would, we believe, undermine the quality of European financial reporting in the international markets; we have made strong representations to this effect to the UK Government.

27 We have sought to enter at an early stage into the European debate on adoption by developing close contacts, at chairman level and below, with other major European national standard-setters, in particular those in France and Germany, and with the European Commission. We are also engaged in Europe in discussions of a more general nature, including consideration of the future role of EFRAG.

THE FUTURE OF UK STANDARDS

28 In my last annual report I explained the Board's strategy for the smooth UK transition to international standards. The Board was mainly concerned, at that stage, with convergence of UK standards in advance of 2005, seeking to achieve a smooth transition for listed companies. Essentially, we planned to transpose several international standards into UK standards in advance of January 2005, in order to allow listed companies to avoid a 'big bang' move to a whole new set of international standards for their group accounts on a single date.

29 Unfortunately, that strategy has been undermined by the slower than expected progress at the IASB and the likely speed of the EU adoption process. The UK Board ideally wants to introduce new UK standards based on IFRS only when it is confident that, once adopted for introduction in Europe in 2005, the relevant IASB standards will survive unchanged for a few more years.

30 There are also legal constraints. Until the EU's Fair Value Directive is brought into effect in the UK, we shall be unable to introduce a standard

incorporating the fair value provisions of IAS 39 (though, as indicated earlier, we still await the definitive revised IAS 39 and may then need further changes to the Fair Value Directive to enable its full implementation). Similarly, until the Government acts on the Modernisation Directive, adopted in June this year to facilitate the convergence of national accounting standards to international standards, various other legal constraints will restrict our freedom to issue UK standards based on international standards.

31 The overall result is that we have not been able to introduce new standards as we had hoped in advance of 2005. Listed companies will now face a 'big bang' change in 2005, at least in relation to their group accounts.

32 There remains the question of how best to manage the relationship from January 2005 between international standards and the continuing UK standards. The DTI announced in July that listed companies will be permitted, but not required, to use adopted IFRS for their individual accounts; other companies and limited liability partnerships will be permitted to use adopted IFRS both for their consolidated and their individual accounts. UK standards will therefore still need to be available for all financial statements other than the consolidated accounts of listed groups. We await the implementing regulations giving effect to the DTI's decision before we can work out the full implications of the July announcement.

33 The ASB's intention is that its UK standards should in the medium term be modelled very closely on the text of the international standards. First, we do not think it is desirable or practicable for the financial reporting community in the UK and Ireland that in the longer run there should be two entirely different sets of standards in parallel for different reporting entities. Secondly, and in due time, we expect international standards to incorporate the best of modern thinking on accounting. We do, however, believe it sensible not to rush the convergence process - not least to avoid two sets of changes where we know that the IASB still intends further changes to its 2005 standards.

34 The Board has recently begun to consider how to take forward a strategy for convergence. There seems no doubt about the direction we want to take, but there is much debate to be had about the extent and timing of the process and we look forward to discussing this with our constituents.

PROJECT REPORTS

35 ASB staff has, during the year, continued to monitor all the work of the IASB, contributing briefing notes to Geoff Whittington in advance of each international Board meeting and exchanging views with IASB staff. Our Board has also discussed each IASB project and given direction to ASB staff. The project reports which follow summarise only those areas which have absorbed substantial staff and Board time this year including, of course, the projects on our own agenda:

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Financial instruments

36 The implementation of IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' will, for most UK and Irish listed companies, be the largest challenge of the move to adopted IFRS at 2005. These standards will have an impact on the group financial statements of almost all listed companies.

37 In summary, the standards require:

- a change in the classification of certain capital instruments between equity and liabilities, and a revised classification of related charges to profit, from those set out in FRS 4 'Capital Instruments';
- amended disclosures of financial instruments from those in FRS 13 'Derivatives and other Financial Instruments: Disclosures';

- a different basis for the recognition and derecognition of financial assets and liabilities arising in complex financing transactions from the requirements of FRS 5 'Reporting the Substance of Transactions';
- all derivatives and many other financial instruments to be marked to market at the balance sheet date; and
- strict limitations on entities' use of hedge accounting techniques to defer recognition in the profit and loss account of the resulting gains and losses to a future accounting period.

38 These international standards were originally published in 1995 and 1998 respectively and were in use when the EU's governments adopted the IAS Regulation in 2002; they have, nevertheless, given rise to considerable recent debate in Europe, as indicated earlier in this report.

39 In June 2002, the IASB issued an exposure draft recommending amendments to the two standards. In March 2003, it organised a series of 'round table' discussions with interested parties. Following subsequent and private discussion with experts from the European Banking Federation, the IASB then issued in August 2003 a further amendment exposure draft, designed to make it easier to achieve hedge accounting for a portfolio hedge of fair value interest rate risk.

40 Meanwhile, the IASB has been debating other aspects of the responses to its 2002 consultation and has made a number of changes to its proposals as a result. Perhaps the biggest change concerns the derecognition of financial instruments. Details of the IASB's revised conclusions in this area were set out in the July 2003 edition of our quarterly newsletter, Inside Track.

41 The main text of the final standards was published in December 2003, with amendments emanating from the August 2003 consultation to be issued in the first quarter of 2004. Subject to EU adoption, the revised IASs 32 and 39 will be effective for 2005, although many aspects of the standards require only prospective application (that is, no comparative information for 2004). These transition issues merit close attention by those who will prepare financial statements under the EU IAS Regulation from 2005 and by the users of such statements.

42 Throughout the year, ASB staff has devoted considerable time to this aspect of the IASB's work. We have given comments to IASB staff at each stage of its debate, and have devoted considerable energy in recent months to reviewing 'pre-ballot drafts', as the IASB has documented its conclusions in final text.

43 The UK Board proposed in FRED 30 (issued June 2002) the adoption into UK standards of the requirements of IAS 32 and the limited adoption of IAS 39. It also issued the IASB August 2003 exposure draft as a supplement to FRED 30. In that latter exposure draft the ASB indicated the factors that it would need to consider before implementing either IAS 32 or 39 in the UK.

Share-based payment

44 In November 2002 the IASB issued its exposure draft (ED 2) on share-based payment, proposing that all entities should be required to recognise an expense, measured at fair value, whenever a share-based payment is made. Having, in the late 1990s, done much of the preliminary thinking for the IASB's work, the UK Board strongly supports the implementation of improved accounting for employee share options, employee share purchase plans and other share-based payments for goods and services. It therefore published simultaneously its own exposure draft (FRED 31) based on the IASB's proposals and proposing the same 2004 implementation date.

45 After consideration of the UK and Irish responses to its exposure draft, the UK Board made representations to the IASB that it should strive to simplify its proposals. The IASB has subsequently reaffirmed its view that share-based payment transactions give rise to an expense that should be measured by reference to fair value. It has, however, concluded that some of its proposals - in particular those on allocating the expense - should be simplified.

46 It is of note that the US Financial Accounting Standards Board (FASB) also has a current project on stock-based compensation. The objective of that project is to co-operate with the IASB to achieve a single basis for recognising the fair value expense, and a US exposure draft is expected to be issued in early 2004. FASB and the IASB are now co-ordinating their discussion of a range of important issues; as a result, it now seems likely that the IASB standard and the US exposure draft will include many similar requirements.

47 Meanwhile, the IASB's timetable for this project has slipped under the pressure of business and the plan is now to issue the final standard in the first quarter of 2004, for implementation in accounting periods beginning in 2005. The UK Board will reconsider the timing and scope of an equivalent UK standard once the IASB's standard is finalised.

Revenue recognition

48 In my report for 2002, I indicated that the ASB was continuing its work on revenue recognition, in order to be in a position to offer interim UK guidance in the event that the international work on this subject was delayed. In February 2003, when it became clear that there was unlikely to be a new international standard for some time, the UK Board issued an exposure draft of an Application Note to FRS 5 'Reporting the Substance of Transactions', proposing guidance on the reporting of turnover. It made clear at this time its intention to seek early use of its proposals as UK standard.

49 Responses to the exposure draft were generally supportive. After careful consideration of the issues raised, the Board published the final Application Note in November, for implementation for years ended on or after 23 December 2003.

50 The Application Note is based on the principle that a seller should recognise turnover only when its performance under a contract with its customers gives rise to either:

- an increase in the seller's assets (such as a debtor); or
- a decrease in the seller's liabilities (usually the release from an obligation arising from payment received in advance).

51 It requires reported revenue to be measured at the fair value of the right to consideration, and provides guidance on the implications of the principles for:

- long term contractual performance;
- separation and linkage of contractual arrangements;
- bill and hold arrangements;
- sales with rights of return; and
- principal and agent.

52 Meanwhile, ASB staff has continued to monitor the revenue recognition work of the IASB and the US FASB. The objective of their joint project is to develop a new standard to replace IAS 18 'Revenue' but it seems that no specific proposals will emerge for some time. The FASB project differs from the UK deliberations on revenue recognition, by

focusing predominantly on gain and loss recognition; the UK's project was, in contrast, primarily concerned with the reporting of turnover.

53 At the request of the IASB, ASB staff contributed a paper which was discussed at the IASB's September meeting. The paper addressed the recognition of revenue under contracts where the customer pays in advance of the seller's performance. It contrasted two approaches: 'wholesale' and 'retail'. Under both the seller recognises a liability. Under the wholesale approach (apparently favoured by the FASB staff) this liability is quantified by reference to the seller's ability to pay another party to assume its obligation to the customer. This will often be less than the amount received, and the balance would be recognised as a gain on inception of the contract. Under the retail approach, which is supported by the UK Board, the liability is initially recorded at the amount received and no revenue is recognised until the seller performs. The retail approach is consistent with the UK Application Note to FRS 5, described above.

Insurance accounting

54 The issues concerning profit or liability recognition for monies received in advance are also apparent in international and UK debates on accounting for insurance contracts. It is noteworthy that the IASB has expressed preliminary views that recognition of a gain at inception of an insurance contract should be strictly limited, despite the wider discussions being explored by IASB and FASB staff in the revenue recognition project.

55 The IASB has divided its major project on insurance accounting into two phases, the first being a transition phase and largely permitting the carry-forward of existing accounting practices at 2005. A 'phase 1' exposure draft to this effect was issued by the IASB in June this year and simultaneously published by the ASB as a consultation paper.

56 Phase 1 seems likely to apply for several years and the UK Board is concerned that the IASB proposes to exempt the reporting of insurance contracts (including reinsurance) from certain basic guidance in other standards, including the requirement that accounting information should be relevant and reliable. The phase 1 exposure draft, if implemented, will allow considerable flexibility in the timing of the recognition and measurement of profits on insurance contracts. The ASB has drawn its concerns to the attention of the IASB, EFRAG, the FSA and others.

57 More positively, the 'phase 1' standard would, if adopted, introduce an increase in reporting disclosures, and therefore assist international

transparency of the various forms of insurance accounting likely to be used in this interim phase. Transparency has long been a concern in the context of insurance accounting.

58 In the UK, staff has throughout the year worked with the ABI to finalise the update of its SORP, of which an exposure draft was published in November 2002. The final SORP was published in November 2003 and includes a number of improvements to the previous (1998) SORP, within the confines of the statutory basis of accounting, including a limitation on early recognition of gains by insurance entities and greater disclosure of liabilities and potential liabilities.

59 ASB staff is now consulting with members of the UK insurance industry, including bancassurers, to build on UK experience with a view to assisting IASB in its deliberations on phase 2 of its project. It is hoped that these consultations may also serve to develop best practice for reporting under phase 1.

Business combinations

60 In December 2002, the IASB published an exposure draft of the first phase of its project on business combinations. At the same time the UK Board issued a consultation paper including the IASB's text, but making clear that the ASB did not propose adoption of the IASB's phase 1 standard in the UK before the complete international package of business combination proposals was available. This seems likely to be some time, not least as this joint project between the IASB and FASB is being tackled in at least three phases.

61 The ASB's reservations on the IASB's phase 1 project, outlined in the preface to the UK consultation paper, were repeated in our response to the international Board. Similar concerns were expressed by a number of UK respondents. The IASB seems likely to meet some of these concerns by subsequent amendments to its proposals on the impairment testing of non-amortised goodwill. It hopes to issue the final standard on this phase of its work by March 2004, to come into effect in 2005.

62 The IASB is expected to publish an exposure draft of the second phase of its project in 2004. Some of its proposals are likely to be particularly controversial. In particular, the IASB considers that the 'full goodwill method' should be adopted in international financial reporting, measuring goodwill as the difference between the fair value of the whole of the acquiree and the fair value of the net assets acquired. This contrasts with the 'purchased goodwill' approach taken under existing UK standards (where goodwill is measured as the difference between the cost

of the investment and the group's share of net assets acquired). It gives rise to different measures of goodwill and minority interest where less than 100% of the acquiree is purchased. The UK Board awaits the final IASB proposals but suspects that there may be both practical and conceptual difficulties with the 'full goodwill' approach.

63 In a complementary step, the IASB is also considering changing its approach to the treatment of minority interests. This involves treating the minority as an equity interest similar to the equity interest of the shareholders of the parent. One consequence is that transactions between the group and minority shareholders (for example, the sale of shares in a subsidiary whilst retaining control) would be portrayed as transactions between owners with neither gain nor loss recognised.

64 These two proposed innovations raise fundamental questions about whether the financial statements are to be prepared, as now, on the basis that the primary focus is reporting to the parent shareholders. The alternative basis, 'the entity approach', has received strong support at the FASB, but is viewed with some concern by many of the other IASB partner standard-setters, including the ASB.

Discontinued operations

65 As part of its project to work towards convergence of IASB and US standards, the IASB published an exposure draft in July on disposal of non-current assets and presentation of discontinued operations. The UK Board simultaneously published a UK exposure draft based on the IASB text. The proposals, based on existing US standards, are quite different from current UK reporting and for example include the presentation of a separate category of assets that are 'held for sale' (subject to certain criteria being met) and possible changes to the measurement of these assets.

66 The key principles of the IASB's proposals include some points on which the UK Board has reservations: in particular the proposals suggest that relatively small parts of a business may be classified as discontinued. Another concern is that some confusion may arise from the early identification of businesses or assets held for sale, which may in due course remain as part of continuing operations. The IASB proposes a standard from this exposure draft for implementation in 2005.

Service Concessions

67 The existing UK accounting requirements on service concessions are largely contained in FRS 5 'Reporting the Substance of Transactions', particularly in Application Note F 'Private Finance Initiative and Similar

Contracts'. There is no equivalent in the IASB's existing literature. This has concerned the ASB and we were pleased that the IASB decided last year that research was needed on the subject. The ASB was asked to lead a group of standard-setters from Australia, France, Spain and the UK to carry out the research.

68 The group reported to the IASB in April this year. It recommended that the IASB should carry out a comprehensive long-term project, in line with its research on leasing (see below). Recognising, however, that this would take some time, the group also recommended that the IASB should ask its International Financial Reporting Interpretations Committee (IFRIC) to clarify how aspects of the existing international literature apply to service concessions. The ASB and IASB supported both these recommendations.

69 Unfortunately, staff resources at IFRIC have not proved sufficient to move the project forward quickly. ASB staff has therefore been endeavouring to assist, and wrote papers for consideration by IFRIC at its September and December meetings. There remains, however, a concern that the project may not achieve sufficient momentum at IFRIC for an interpretation to be issued (and adopted by the EU) in time for 2005 financial statements.

Comprehensive income

70 The ASB and IASB worked together throughout 2002 on this project, whose objective is to develop a single statement of financial performance to report total gains and losses for the period. It is primarily concerned with determining the structure of the statement and the allocation of items of comprehensive income within that structure; it does not address issues of recognition and measurement.

71 In early 2003, ASB and IASB staff conducted field tests on the proposals - involving a substantial number of analysts and major companies in the UK, as well as similar constituents in other territories of IASB partner standard-setters. As was to be expected at this relatively early stage of research, reactions to the proposals were mixed: major concerns were expressed in continental Europe and in Japan, mainly focusing on the shift in emphasis away from realised profit and net income. The investment community was generally supportive, however, and the field visits were useful in identifying issues for further study and development.

72 As the year progressed it became increasingly clear that the IASB lacked the agenda time to give substantive further consideration to the project before the 2005 deadline.

73 The project has therefore now been given a more relaxed timetable. A discussion paper is planned for 2004. The two Boards are also engaging in discussions with the FASB, which is at the research stage of a similar project of its own, to ensure that all relevant considerations are reflected in the discussion paper.

Consolidations

74 In 2001, the IASB commissioned the ASB to carry out research on policies used around the world for consolidation and for the inclusion of Special Purpose Entities (SPEs) in group financial statements. ASB staff reported on this project in May 2002, arguing for a universal system of consolidation based on whether one entity controls another with a view to benefit (the basis of the UK standard, FRS 2).

75 The IASB has recently returned to this topic and confirmed the approach of its existing standard (IAS 27) that consolidation should reflect control. Indications are that the IASB will next year start to further develop its control-based consolidation model. It has tentatively decided that the concept of control should require satisfaction of three criteria:

- the ability to set strategic direction and to direct financing and operating policy and strategy (the 'Power Criterion');
- the ability to access benefits (the 'Benefit Criterion'); and
- the ability to use such power so as to increase, maintain or protect the amount of those benefits.

76 The assessment of control is to be based on the circumstances of each case. The international Board has tentatively agreed that irrespective of the form of control, if the control criteria are satisfied, consolidation should be required. This would include the holder of less than a majority interest being deemed to be in control if the remaining holdings are widely dispersed - a notable departure from the current concepts enshrined in US accounting standards.

77 As noted above, IAS 27 and the related guidance on SPEs (SIC 12) include concepts which are not unlike these recent IASB decisions, though the current implementation guidance is far from detailed. The decisions should, however, enable UK and Irish companies facing the move to adopted IFRS in 2005 to be reasonably confident that the IASB's future development of its standards may be in line with current UK and IASB consolidation policies.

Leasing

78 The IASB has shown strong interest in ASB's preliminary work on a new accounting standard for leasing. Building on the UK Board's Discussion Paper 'Leases: Implementation of a New Approach', the aim is to develop a single method for accounting for all leases, rather than maintain the current approach under which radically different accounting treatments are applied to finance and operating leases on the basis of a distinction which is arbitrary and inevitably problematic.

79 However, the complexity of many leases poses significant challenges in determining and measuring the assets and liabilities that arise from them, for example where a lease contains options to renew coupled with a guarantee by the lessee of the residual value of the equipment.

80 The UK Board has been developing its views on leasing over the last couple of years. The IASB has, however, lacked agenda time until May of this year to begin to consider the project. In that month, ASB staff presented to an IASB meeting a survey of leasing issues and a project plan, under which the two Boards might work together on the development of a new leasing model over the next three years. A further paper was presented at the IASB's November meeting.

81 We have since discussed the same concepts with national standard-setters in Europe, to obtain their reactions to the project proposal and to encourage their participation. Typical leasing arrangements vary from country to country and ASB staff is keen to ensure that it understands the variety of tax and legal structures of leases, as it develops its further thoughts.

Measurement

82 Modern accounting standards frequently permit the use of measurement bases other than historical cost. For example, fixed assets may be revalued; standards on impairment require a balance sheet date valuation in some circumstances and financial instruments are increasingly reported at fair value.

83 There is, however, little consensus as to what exactly should be the alternative to historical cost. The ASB has consistently been of the view that the general use of selling prices would not be appropriate, and that there remains a case in many circumstances for the use of current acquisition values.

84 During 2003, the ASB continued its active participation in two international projects on this issue. One was the work of the IASB Revaluation Group (a group of standard-setters, led by New Zealand, and including members from Australia, South Africa and the ASB, as well as IASB Board members) on the revaluation basis to be specified in IAS 16 'Property, Plant and Equipment'.

85 The Group's agreed recommendations were presented to IASB and other national standard-setters in April. It is disappointing that the revised IAS 16, published in December, does not include the results of this work, nor are the IASB's future plans on this subject clear.

86 The other international project is work led by Canada on the conceptual basis to be used in the measurement of assets and liabilities. We have commented extensively on drafts and participated in discussion of them at meetings with other national standard-setters. The key to progress appears to be developing an understanding of the relationship between the fair value, cost and deprival value approaches and the circumstances in which these might lead to different results.

Small and medium sized entities ('SMEs')

87 The year saw some developments in the IASB research project on the application of international accounting standards to small and medium sized entities. The IASB's advisory panel - on which ASB member Isobel Sharp, Chairman of the Board's Committee on Accounting for Smaller Entities serves - met in April and the subject was discussed at the meeting of world standard-setters in September.

88 It was clear in discussion with standard-setters from the 39 countries represented at this meeting that there is strong support for the IASB to take the initiative to develop a reporting framework for SMEs. Like the UK's Financial Reporting Standard for Smaller Entities, this will probably involve a greater focus on reducing requirements for presentation and disclosure than on changing the bases for recognition and measurement.

Operating and Financial Review

89 In January 2003 we issued an update of the Statement on the Operating and Financial Review (OFR), which was first published in 1993. The updated text was welcomed by the CBI and by representative bodies of institutional investors. The Financial Services Authority called for all listed companies "to have regard to this Statement when preparing their next annual reports". Staff has, since then, had many discussions with parties interested in extended corporate reporting on how their particular areas of interest might be incorporated within the OFR.

90 In its 2002 White Paper, the Government put forward proposals to require large companies to publish an Operating and Financial Review and, where material, to include information relating to policies and performance on employee, environmental, social and community issues and other matters affecting the company's reputation.

91 The Government set up a working group, on which I serve, to consider guidance on how directors can assess whether such topics are material to their company and hence must be included in an OFR. The group published a consultation document in June and expects to issue its final report soon. It is understood that the Government hopes to introduce legislation to implement its proposals on the OFR at an early date.

92 Meanwhile, the IASB has initiated a research project on the potential development of an 'international OFR'. This project is being led from New Zealand, with the active participation of the ASB and partner standard-setters in Canada and Germany.

THE WORK OF THE BOARD'S COMMITTEES*Urgent Issues Task Force*

93 In March, the Urgent Issues Task Force (UITF) issued Abstract 36 'Contracts for Sales of Capacity', following the publication of a consultation draft in November last year. This addressed:

- the limited circumstances in which a contract for the right to use network capacity should be reported as the sale of an asset (with immediate income recognition rather than recognition over the life of the contract);

- the limited circumstances in which proceeds should be shown as turnover (and therefore included in operating profit) rather than as a fixed asset disposal; and
- the rare circumstances in which exchanges of capacity (capacity swaps) might give rise to the recognition of turnover or disposal gains.

94 In May, the UITF published a draft Abstract on Treasury Shares. New regulations, The Companies (Acquisition of own Shares) (Treasury Shares) Regulations 2003, came into effect in December allowing certain companies to purchase their own shares and hold them in treasury without cancelling them. Companies may at any time sell such shares for cash, use them for an employee share scheme or cancel them. The UITF was keen to ensure that UK accounting requirements were in place by the time companies were able to take advantage of the new regulations.

95 Responses to the draft raised questions about the scope of the proposed abstract. The UITF therefore initiated a supplementary consultation in July, clarifying its view that the accounting proposals should apply to all purchases and sales of own shares including, in consolidated accounts, where the holding company's shares are held by subsidiaries.

96 Abstract 37 'Purchases and Sales of Own Shares' was issued in October and reflects the views set out in the July consultation. It requires a holding of an entity's own shares to be accounted for as a deduction in arriving at shareholders' funds, rather than being recorded as assets. Transactions in such shares are similarly recorded in shareholders' funds and do not give rise to gains or losses. This accounting treatment is in line with that set out in International Accounting Standards and takes effect for accounting periods ended on or after 23 December 2003.

97 Parallel proposals were also issued in May, to change Abstract 13 'Accounting for ESOP Trusts' from requiring shares in an ESOP trust to be recognised as assets to require them to be deducted in arriving at shareholders' funds. Most respondents agreed with this proposal; questions were raised, however, as to the consequential effect on Abstract 17 'Employee Share Schemes'. A supplementary consultation note on amendments to Abstract 17 was issued in October. In December, the UITF published Abstract 38 which supersedes Abstract 13 and makes amendments to Abstract 17 to take mandatory effect for accounting periods ending on or after 22 June 2004.

98 In May, the UITF also issued a draft Abstract on accounting for emission rights. It addresses the accounting by participants in an emissions trading scheme that applies a 'cap and trade' model. The UK's Emissions Trading Scheme, launched in 2002, is an example of such a scheme. Participants accept a cap on their carbon dioxide emissions and receive tradable emission allowances corresponding to the amount of the cap. An EU-wide scheme will start in 2005.

99 The proposed Abstract presents the text of a draft Interpretation from the IASB's International Financial Reporting Interpretations Committee (IFRIC), together with the changes that the UITF proposed to reflect accounting requirements in the UK where they differ from International Accounting Standards. It proposes that a participant should recognise separately an asset (for emissions allowances held), a liability (for the obligation to deliver allowances for emissions that have been made) and a government grant (where allowances are allocated by government for less than fair value).

100 In the light of comments received, the UITF has begun to explore a modified model where each of the components is measured by reference to the fair value of allowances, with changes in value reported in the profit and loss account. No decisions have yet been taken, however. ASB staff has provided papers summarising the UITF's discussion on a 'fair value' approach to the staff of IFRIC. The UITF will monitor the progress of IFRIC's debate, before deciding on the next steps.

*Financial Sector and Other Special Industries Committee
Public Sector and Not-for-Profit Committee*

101 The Financial Sector and Other Special Industries Committee (FSOSIC) and the Public Sector and Not-for-Profit Committee (PSNC) are chaired respectively by Board members Isobel Sharp and John Smith. The committees have continued, during 2003, their important work in advising the Board on the maintenance of Statements of Recommended Practice (SORPs) by existing SORP-making bodies. The output of this work in 2003 is reflected in Appendix 3.

102 SORPs have had an important role in the UK system of accounting pronouncements for many years. The SORP on Investment Trusts, for example, is considered by many to provide a useful and necessary reporting regime for that sector. The SORP model is also widely used in the public benefit sector - for example in financial reporting by local authorities, housing associations and charities. Although adherence to a

SORP may not be mandatory, the accounting and business communities expect them to be followed and the ASB's standard FRS 18 'Accounting Policies' requires reporting entities to disclose whether or not they follow the relevant SORP.

103 Looking ahead, the DTI's proposals to introduce, from 2005, a choice between UK standards and adopted IFRS will have implications for the SORP regime. For companies choosing adopted IFRS, member states may not be able to mandate financial reporting guidance additional to that issued by the IASB and adopted by the EU. But the IASB has not yet had time to consider standards or guidance for particular sectors, and IASB standards are not designed to apply to some reporting entities such as those in the public benefit sector. The implications for SORPs will therefore need careful consideration if we are to avoid creating a gap.

*Statement of Principles for Financial Reporting:
Proposed Interpretation for Public Benefit Entities*

104 In addition to its work on SORPs, the PSNC has spent considerable time and energy debating whether and how the long-established fundamentals of financial reporting should be applied in the not-for-profit arena. In May, the Board published as a Discussion Paper the fruits of its work: the 'Statement of Principles for Financial Reporting: Proposed Interpretation for Public Benefit Entities'.

105 This draws substantially on the ASB's Statement of Principles for Financial Reporting, published in 1999, which was written primarily with profit-orientated entities in mind. The Discussion Paper considers that in many cases the fundamentals of accounting are equally applicable to both government entities and charities; it does, however, suggest in some cases a re-expression of the principles to make them easier to apply.

106 A key consideration in the project is how to define the entities in question. The Paper proposes an all-embracing new definition for the sector: public benefit entities, which have a primary objective to provide goods or services for the general or social benefit, rather than a financial objective relating to returns to equity shareholders.

107 The proposed interpretation provoked a widespread response, not only from UK public benefit entities and their advisors, but also from overseas. The PSNC is now carefully considering all the responses received, with a view to proposing amendments and additional guidance for consideration by the Board in due course. One area which appears most controversial is the definition of liabilities and in particular whether it is possible to find a robust boundary in accounting terms between

general policy statements of intention (for example by government or charities) and constructive obligations from which an entity could not realistically withdraw.

108 The Board is keenly interested in the outcome of this project, which is already provoking international interest. We have noted in particular that the IASB has made clear that its standards are not designed to apply to not-for-profit activities. As its standards increasingly become the model for international financial reporting, however, we consider it important to provide a 'bridge' from profit-orientated reporting to the public benefit sector.

Committee on Accounting for Smaller Entities

109 The Committee on Accounting for Smaller Entities (CASE) is also chaired by Board member Isobel Sharp. It has a key role in supporting the Board in our interface with the IASB's project on SME accounting, described earlier in this report. Isobel, in particular, is a member of the advisory panel on this work.

110 Earlier this year, CASE advised the Board that no update of the UK Financial Reporting Standard for Smaller Entities (FRSSE) was needed in 2003. It has since started work to consider the implications for UK smaller entities of the move towards adopted IFRS from 2005.

GETTING THE JOB DONE

111 In describing the workload of the Board and its committees this year, I have many to thank for their considerable support and for the unceasing energy they bring to our wide-ranging agenda.

112 Our Board members give us huge amounts of their time, not only in our lively (and sometimes heated) debates but also in their personal research of the complex issues we put before them. Their practical business knowledge and wide international experience bring much to our discussions, enabling us to contribute successfully to the global agenda. We were sorry to lose David Allvey, John Coombe and Ken Wild from the Board this year. Between them, they have over 25 years experience at the ASB and they will be sorely missed. On a more positive note, we have been delighted to welcome Jon Symonds, CFO of AstraZeneca, and look forward to the arrival of Mike Ashley, partner at KPMG.

113 I must also pay tribute to the members of the Board's committees, without whom we could not have sustained our heavy and wide-ranging workload. I thank in particular those who have left the committees over the last twelve months: Eric Anstee, James Carty, Alexis Chapman, Derek Harris, Robert Law and Allister Wilson; and I welcome Peter Chidgey, Howard Evans, Guy Jubb and Robert Overend to the UITF; Richard Bray and Richard Laughlin to PSNC; and Claire Adams and Richard Roberts to CASE.

114 The people on whom the organisation ultimately depends are, of course, the staff. It is their talent and enthusiasm that enable us to maintain the UK's strong presence in today's international standard-setting environment and make us welcome partners in the IASB's deliberations. Our small team is managing an ever-increasing workload and I am grateful for their energy and dedication.

115 Very special thanks are due to Allan Cook, the Board's Technical Director since it was established in 1990; he brings real wisdom and unrivalled knowledge to all our deliberations and I am constantly grateful for his advice. He is standing down as Technical Director from the end of this year, but I am delighted that he will continue to work with us as 2005 approaches and will also keep us in close touch with the work of EFRAG in Brussels. Andrew Lennard, formerly Director of Operations, takes over as ASB Technical Director from January 2004.

116 As is clear from this report, the shifting of power in the making of standards brings new and demanding challenges for national standard-setters. Those we have faced in 2003 seem likely to be repeated in the years ahead - and new areas of work seem likely to emerge. It is good to know that we do not face these challenges alone. The resident Holborn Hall team, the members of the Board and its committees, and our wider stakeholders in UK and Irish financial reporting work extraordinarily well together. I thank every one of them for their contribution this year - and I depend on the same for 2004.

MARY KEEGAN

THE FINANCIAL REPORTING
REVIEW PANEL

3

CHAIRMAN'S REPORT

FINANCIAL REPORTING REVIEW PANEL

CHAIRMAN'S REPORT

1 I am very aware of the challenges that face the Financial Reporting Review Panel as it responds to a number of domestic initiatives and international developments that look to expand its activities and its remit. The current reactive approach is in the process of being replaced by a programme of proactive review; in the medium term, the scope of the Panel is to be extended to include other financial information published by listed and certain other companies; and for the longer term, the Government is considering whether to give the Panel some responsibility for the enforcement of accounting requirements in the financial information of a range of other entities currently outside its scope.

2 If, in terms of its longer term remit and operational procedures, the watchword for the Panel appears to be that of 'change', the key to successful transition lies in maintaining, within that change, the key principles that have supported the Panel's success in the past.

PANEL ORIGINS

3 The current regime for the setting and enforcement of accounting standards in the UK was established in line with recommendations made by the Dearing Committee, which was set up in the wake of a number of corporate failures and scandals involving poor accounting and reporting in the 1980s. There was general acceptance that change was needed to address concerns about prevailing accounting practices in order to support effective financial markets and to improve the quality of information available to shareholders.

4 The Financial Reporting Review Panel was set up to provide robust enforcement of the newly-emerging standards issued by the Accounting Standards Board, which were needed to strengthen the framework for financial reporting in the UK.

5 The Panel's objective, then as now, was to contribute to the enhancement of good financial reporting in the UK through enforcement of the accounting requirements of the Companies Act 1985, including applicable accounting standards, in the annual financial statements of public and large private companies.

PROACTIVITY

6 The widely publicised corporate collapses in the US over the last couple of years, precipitated by the demise of Enron and followed by World.com and others, had a significant and immediate impact on global markets and investor confidence. The UK Government responded by setting up the Co-ordinating Group on Audit and Accounting Issues (CGAA) to review the adequacy of the UK regulatory regime. CGAA was to seek ways of strengthening the roles of key players within the UK regulatory framework and, where practicable, to consider increasing the effectiveness of a system that is generally well-respected and that is perceived to work.

7 In response to the CGAA's interim report, Ian Brindle, Deputy Chairman of the Panel, led a small group ('the Group') to consider how best an element of proactivity might be introduced into the Panel's procedures. The Group reported to CGAA on the understanding that the Government initiatives did not envisage changing the overall shape of the current regulatory regime nor that of its various components.

8 CGAA considered the Group's report together with submissions from other representatives of regulatory, accountancy and stakeholder groups. The Secretary of State formally reported on behalf of the CGAA in January this year, recommending that the Panel should develop a proactive role for the enforcement of accounting standards in which the FSA should play an active part. The Government also announced further work to determine whether a legal gateway could be created to enable the Inland Revenue to refer matters of potential interest to the Panel for further review.

Risk-based approach to proactivity

9 Following discussions with the Financial Services Authority (FSA), the Panel has agreed a Memorandum of Understanding to facilitate co-operation and co-ordination between the two authorities. The FSA will provide the Panel with their annual Financial Risk Outlook and a quarterly letter summarizing other information that, in the opinion of FSA, is likely to be of interest to the Panel in its risk assessment process and which it has obtained either by virtue of its regulation of authorised persons or in its capacity as UK competent authority for listing.

10 In consultation with members of the Panel and consistent with CGAA recommendations, the Panel has determined an approach to the proactive review of financial information. The approach has been reviewed by DTI, FSA and HMIT. The Deputy Chairman, Ian Brindle, is currently communicating the approach to interested groups representative of the broader financial reporting community.

11 The UK has by far the greatest number of companies listed on a regulated market in the EU. The Panel intends stratifying the companies under its remit to allow an efficient risk-based approach founded on the two principal criteria of the probability of mis-statement occurring within a set of annual financial statements and the potential impact of that mis-statement on the confidence and economic decisions of the investing and broader stakeholder community. Resources will be focused on the financial information of those companies with a greater potential for market impact. The financial information selected for review will include, but will not be restricted to, full sets of company accounts. The risk analysis will also drive targeted reviews of specific industry issues and compliance with selected accounting requirements.

12 It is important that the Panel, in proactive mode, continues to take account of the concerns of the broader financial reporting community, which has been a key principle of its modus operandi as a reactive body. The Panel will ask a representative stakeholder group to help it consider the impact of macro-economic events on industry and sector groups, and to assist the Panel in its identification of areas of contemporary risk. The specific criteria to be applied in the selection process are dynamic and will change as issues emerge and events take place in the economic and financial environment as indicated by FSA and other expert advice.

13 The Panel is presently testing its systematic approach by selecting accounts and issues for review. Experience gained during 2003 has been helpful in developing the internal and communication processes and determining the number of additional staff and type of expertise that might be needed in the future.

Managing expectations

14 No regulatory system of enforcement can ensure the infallibility of a financial reporting regime. The UK framework, even when taken as a whole - that is including directors, auditors and audit committees each fulfilling their various responsibilities within their separate roles - cannot guarantee that accounts are prepared in accordance with applicable accounting requirements, nor that those accounts are free from fraud or error.

15 The Panel's contribution to the UK system of financial enforcement is significant but limited. First, the Panel reviews accounts for apparent compliance with accounting requirements. It does not set out to test the fundamental assertions on which the accounts are based, nor to prove the accuracy of the reported numbers. Second, the Panel will not review all accounts within its scope in any one reporting season. Its reviews will be

conducted on a sample basis and will include partial reviews of accounts where the focus is on an industry issue or, for example, a particular aspect of an accounting standard. Finally, no enforcement system can be relied upon to prevent or detect fraud which is specifically designed to overcome controls and for which there is no effective regulation. Even when operating on a proactive basis, the Panel will not be able to give the kind of broad reassurance that some may be seeking about compliance by UK companies as a whole. The deterrent effect of the Panel's existence and public knowledge of its proactive stance however, should not be underestimated.

16 As previously reported, Germany and Sweden have shown particular interest in the Financial Reporting Review Panel as a model for the enforcement of accounting standards. I was pleased to hear that in April, Sweden established a body which adopts the key principles of the UK Panel. More recently, the German Government announced that an independent Panel of experts is to play a key role in the enforcement of accounting standards of companies listed in Germany.

European Developments in financial regulation

17 Elsewhere, Mary Keegan has reported on the implications for UK preparers and auditors of the EU Accounting Regulation which is intended to spread transparent financial reporting across member states. While acknowledging that enforcement is a national responsibility, the Commission asked the Committee of European Securities Regulators (CESR) to encourage a common approach to the enforcement of those standards across member states.

18 The Sub-Committee charged with this task, CESRfin SCE, published Standard 1, 'Enforcement of Standards on Financial Information in Europe' in March. The Standard sets out a number of principles relating to the role, powers and methodology of enforcers of financial information with which CESR members are encouraged to comply. Since May, the Panel has attended CESRfin SCE meetings as technical adviser to the FSA. This gives the Panel the opportunity of feeding its enforcement experiences directly into debate with EU peer bodies and of influencing the development of subsequent Standards.

19 The sub-committee has recently published a second draft Standard which proposes a mechanism for ensuring that private independent bodies such as the Panel will have the opportunity of participating fully with securities regulators in the further development and co-ordination of a harmonised approach to regulation in the EU. Standards issued by CESR are not legally binding on members who are required to adopt them

on a 'best efforts' basis. As the member state with the largest number of listed companies in the EU, the UK Government is keen to comply with the recommendations.

20 The Panel hopes to continue to influence and contribute to the work of the sub-committee to ensure that the principles of enforcement encouraged at national level will deliver robust systems of enforcement across all member states. More generally, it also hopes to co-operate with and assist other countries setting up Panel-style enforcement arrangements.

Proposed legislation

21 Under the Companies (Audit, Investigations and Community Enterprise) Bill, which was introduced on 3rd December 2003, the remit of the Panel can be extended to cover financial information, other than annual accounts, published by entities that have an instrument listed on a UK market and where mandatory accounting requirements may apply. This will, for example, include interim reports, directors' reports and operating and financial reviews.

22 The Bill also gives power to extend the Panel's remit to include the financial information of certain UK entities whose securities are listed on a UK market but which are not companies and that of overseas companies who have a UK listed instrument.

23 The Panel has no power to compel companies to respond to its enquiries. It has, until now, relied on the willingness of companies to co-operate with the Panel. Consistent with the minimum expectation of CCSRfin Standard 1 and in line with the requirements of EU Directives, the Bill proposes to give the Panel a legal power to require supplementary information from issuers and their auditors. The Panel hopes however that the consensual approach that has characterised its enquiries to date will still continue under a proactive regime and that it will not need to resort to this authority to discharge its responsibilities.

24 The Panel has always been concerned to satisfy the needs of the financial reporting community it was established to serve and to whom it is accountable. The UK Government's objective of providing a regulatory system to meet the demands of the 21st Century have a significant impact on the future role and remit of the Panel.

25 Increased expectations clearly have implications for the Panel's required resources in terms of funding and staffing levels. To date, the Panel has worked with minimal staff and with Panel members volunteering their time and valuable experience freely. Having recruited two highly expert reviewers during the year, the Panel expects very shortly to make three further appointments.

THE PANEL YEAR

26 Over the past year the Panel has had unprecedented involvement in a range of discussions and debates about the principles, nature and methodology of enforcement of accounting requirements, both on a domestic and international level. It has also continued to receive and consider complaints about specific set of accounts which it has reviewed in accordance with its Operating Procedures which were revised on 29 October to reflect the Panel's ability to operate proactively in respect of annual accounts.

Operating statistics

27 At the beginning of the year the Panel had 8 cases under enquiry. A further 51 sets of accounts were drawn to its attention during the period; most of which were found to have no substance or to be outside the Panel's remit or jurisdiction. Of the cases taken forward, corrective action was announced in respect of two companies.

28 In the case of Finelot plc, the Panel found that certain items capitalised as development costs under SSAP 13 did not satisfy the criteria for 'development' as defined within the standard and that they should have been written off as incurred, as required by UITF Abstract 24.

29 In the case of Kensington Group plc, the Panel found that, as they satisfied criteria for quasi-subidiaries, securitisation companies of the group should have been fully consolidated in the consolidated balance sheet and cash flow statement using a linked presentation, as required by FRS 5.

30 Copies of these press notices are available on the Panel's website or from Holborn Hall.

31 In addition to the accounts drawn to its attention during the year, the Panel also initiated reviews of the accounts of over 30 listed companies broadly in accordance with its proposed general risk approach. It is premature to make any comment on the Panel's findings in respect of these sets of accounts.

32 As I have said in previous reports, the success of the Panel lies partly in the respect in which its members are held by the reporting community it serves. This year, a founder member, David Mitchell, stepped down from service. I thank him for the years of experience he has offered both me and my predecessors.

33 2003 has been a challenging year that has made heavy demands on us all. I am especially thankful for the support of the Deputy Chairman, Ian Brindle, who chaired the Panel Group on Proactivity and who has been closely involved with a range of discussion and debates with Government and other regulators. I also thank his fellow group members, Martin Eadon, John Grieves, David Mallett, Andrew Popham and George Rose for their continued work on proactivity during the year.

CONCLUDING REMARKS

34 This is my fourth and final report as Chairman of the Panel. In early 2004 my place will be taken by a new Chairman, to be appointed after a rigorous selection process including public advertisement. It is already clear that the role will be considerably more active than when I started in 2000.

35 I have enjoyed my time at the Panel and have been extremely lucky to work with such excellent colleagues, as well as two excellent Deputy Chairmen. Ann Wilks as Secretary and Carol Page as Assistant Secretary and now Director, Panel Operations have provided much-needed support and advice. Their workload, particularly during 2003, has been enormous, but they have coped with great skill and good humour. I believe that I shall leave the Panel in good heart to cope with the future challenges.

RICHARD SYKES



4

APPENDICES

FINANCIAL REPORTING COUNCIL

APPENDIX 1

MEMBERSHIP OF THE BODIES AT 31 DECEMBER 2003

THE FINANCIAL REPORTING COUNCIL

Chairman

*†Sir Bryan Nicholson

Deputy Chairmen

*†Sir John Egan
President of the CBI

*David Illingworth

Chairman of the Consultative
Committee of Accountancy Bodies
President of the Institute of Chartered
Accountants in England and Wales

Members

Mary Keegan
(ex officio)

Chairman of
the Accounting Standards Board

Richard Sykes QC
(ex officio)

Chairman of
the Financial Reporting Review Panel

†Charles Allen-Jones

Formerly Senior Partner,
Linklaters & Alliance

Mike Barnes

Head of Technical Development,
Audit Commission

Scott Bell CBE

Formerly Group Managing Director,
The Standard Life Assurance Company

Sir Victor Blank

Chairman, GUS plc and
Chairman of Trinity Mirror plc

Sir John Bond

Group Chairman, HSBC Holdings plc

Martin Broughton

Chairman, British American Tobacco plc

†Sir David Clementi

Chairman, Prudential plc

Don Cruickshank	Chairman, SMG plc
Michael Foot	Managing Director, Deposit Takers & Markets Directorate, Financial Services Authority
Stephen Haddrill	Director General, Fair Markets Group, DTI (Government nominee)
*†Sir Derek Higgs	Senior Adviser in the UK, UBS Warburg
Douglas Kerr	Group Finance Director, CPL Industries Ltd
Rory Murphy	Joint General Secretary, UNIFI
†Paul Myners	Chairman, Guardian Media Group plc
Richard Pearson	Senior Partner, PKF
†Colin Perry	Chairman, LTE Scientific Ltd
Ian Plaistowe	Formerly Chairman, Auditing Practices Board
Sir Nigel Rudd	Chairman, Boots Group PLC and Pilkington plc
Vincent Sheridan	Chief Executive, VHI Healthcare
†Sir Robert Smith	Chairman, The Weir Group PLC
Rosemary Thorne	Group Finance Director, Bradford & Bingley plc
*Graham Ward	Partner, PricewaterhouseCoopers
<i>Observers</i>	
Sir John Bourn KCB	Comptroller & Auditor General, National Audit Office
Peter Brierley Bank of England (Bank of England nominee)	Head of Domestic Finance Division,

Sir Andrew Likierman

Managing Director, Financial
Management, Reporting and Audit,
HM Treasury, and Head of the
Government Accountancy Service

Paul Druckman

Deputy President, the Institute of
Chartered Accountants in England
and Wales

Secretary

Ann Wilks CBE

NOTE: The Appointments Committee comprises the members indicated by *. The Working Group on the Combined Code comprised the members indicated by †.

In 2003 the following ceased to be members of the Council:

Peter Wyman (formerly a deputy chairman)

David Bishop

David Challen CBE

Hilary Cropper CBE

THE ACCOUNTING STANDARDS BOARD

Chairman (full-time)

Mary Keegan

Technical Director (full-time)

Allan Cook CBE² - to 31 December 2003

Andrew Lennard¹ - from 1 January 2004

Members (part-time)

Mike Ashley ¹	Partner, KPMG LLP
Douglas Flint	Group Finance Director, HSBC Holdings plc
Huw Jones	Director of Corporate Finance, M&G Investment Management Limited
Roger Marshall	Partner, PricewaterhouseCoopers LLP
Isobel Sharp	Partner, Deloitte & Touche LLP
John Smith	Director of Finance, Property and Business Affairs, British Broadcasting Corporation
Jonathan Symonds	Chief Financial Officer, AstraZeneca plc
Ken Wild ²	National Director - Assurance & Advisory Services, Deloitte & Touche LLP

Observers

Sir Andrew Likierman	Managing Director, Financial Management, Reporting and Audit, HM Treasury, and Head of the Government Accountancy Service
Bernadette Kelly	Director, Company Law and Investigations, Department of Trade and Industry
Professor Geoffrey Whittington CBE	Liaison member of the International Accounting Standards Board

Secretary

Charles Bridge

In 2003 David Allvey and John Coombe ceased to be members of the Board

¹Becomes a member of the ASB on 1 January 2004

²Ceased to be a member of the ASB on 31 December 2003

THE URGENT ISSUES TASK FORCE

Chairman (non-voting)

Mary Keegan

Members

Professor

Dublin City University

Patricia Barker

Paul Boyle

Chief Operating Officer, Financial Services Authority

Peter Chidgey

Partner, BDO Stoy Hayward LLP

David Devlin

Partner, PricewaterhouseCoopers, Ireland

Howard Evans

Finance Director, Misys plc

Peter Holgate

Senior Accounting Technical Partner,
PricewaterhouseCoopers LLP

Michael Hughes

Chairman of Assurance, KPMG LLP

Guy Jubb

Investment Director, Head of Corporate Governance,
Standard Life Investments

Marian MacBryde

Director, Makinson Cowell Limited

Christopher Nunn

Formerly Professional Standards Partner, Andersen

Robert Overend

Partner, Ernst & Young LLP

Richard Piper

Formerly Finance Director, W S Atkins plc

Brian Shearer

Technical Partner, Grant Thornton

Andy Simmonds

Technical Partner, Deloitte & Touche LLP

Jonathan Southern

Director of Accounting, Diageo plc

Technical Director

Hans Nailor

Secretary

Charles Bridge

In 2003 Eric Anstee, James Carty, Jonathan Symonds and Allister Wilson ceased to be members of the UITF.

THE FINANCIAL SECTOR AND OTHER SPECIAL INDUSTRIES COMMITTEE

Chairman

Isobel Sharp Member, ASB and Partner, Deloitte & Touche LLP

Members

David Cairns Senior Visiting Fellow,
London School of Economics and formerly
Secretary General of the IASC

Deborah Chesworth Manager, Prudential Standards Division,
Financial Services Authority

Julian Hance Group Finance Director,
Royal & SunAlliance Insurance Group plc

Rajan Kapoor Group Chief Accountant,
Royal Bank of Scotland Group

James MacLeod Chairman, Martin Currie High Income Trust plc
and Collective Assets Trust plc

Lynn Percy Partner, KPMG LLP

Derek Stevens Formerly Chief Financial Officer,
British Airways plc

Observer

Andrew Watchman Company Law and Investigations Directorate,
Department of Trade and Industry

Secretary

Janie Crichton

In 2003 Robert Law ceased to be a member of the FSOSIC.

THE PUBLIC SECTOR AND NOT-FOR-PROFIT COMMITTEE

Chairman

John Smith Member, ASB and Director of Finance, Property & Business Affairs, British Broadcasting Corporation

Members

Mike Barnes Head of Technical Development, Audit Commission

Richard Bray Financial Accountant, Cancer Research UK

Stephen Burgess National Director, Life Education Centres

David Creed Chairman, The Housing Corporation Limited

Martin Daynes Director, National Audit Office

Virginia Grace Group Director of Finance, Moat Housing Group

Ieuan Griffiths Director of Finance & Strategy,
Driver and Vehicle Licensing Agency

Michael Hathorn Partner, Moore Stephens UK

Professor
Richard Laughlin Professor of Accountancy, Kings College London

Sean Nolan Director of Corporate Resources,
East Sussex County Council

John Stanford Assistant Director Technical and International,
Chartered Institute of
Public Finance and Accounting

Ken Wild¹ Member, ASB and National Director -
Assurance & Advisory Services, Deloitte & Touche LLP

Observers

Raymond Jones Policy Accountant,
Charity Commission for England and Wales

David Loweth Head of Central Accountancy Team, H M Treasury

Secretary

Jenny Carter

¹Ceased to be a member of the PSNC on 31 December 2003

THE COMMITTEE ON ACCOUNTING FOR SMALLER ENTITIES

Chairman

Isobel Sharp
Member, ASB and
Partner, Deloitte & Touche LLP

Members

Claire Adams
Finance Director, ECT Venues Limited

Alan Donaldson
Partner, Scott-Moncrieff

David Finch
Formerly Group Finance Director,
Spaldings Ltd

Paul Flanagan
Head of Risk, Euler Trade Indemnity Plc

Melvyn Howell
Formerly Senior Manager, Midland Bank Plc

Liam McQuaid
Managing Partner, Duignan Carthy O'Neill

Dr Richard Roberts
Head of SME Research, Barclays PLC

Danielle Stewart
Senior Partner, Warrener Stewart

Observer

Valerie Carpenter
Assistant Director, Company Accounting &
Disclosure, Department of
Trade and Industry

In 2003 Derek Harris ceased to be a member of the CASE.

THE FINANCIAL REPORTING REVIEW PANEL

Chairman

Richard Sykes QC

Deputy Chairman

Ian Brindle

Members

Rupert Beaumont Formerly Partner, Slaughter and May

Sir John Bourn KCB Comptroller & Auditor General,
National Audit Office

Stephen Box Finance Director,
The National Grid Group plc

Michael Brindle QC Barrister

Richard Delbridge Formerly Group Chief Financial Officer,
NatWest Group

Martin Eadon Partner, Deloitte & Touche

John Grieves Formerly Senior Partner, Freshfields

Gordon Hamilton Partner, Deloitte & Touche

Andrew Higginson Finance Director, Tesco PLC

Robert Hildyard QC Barrister

Nigel Macdonald Partner, Ernst & Young

David Mallett Formerly Group Head of Finance,
Standard Chartered Bank

Ron Paterson Formerly Partner, Ernst & Young

Graham Pimlott Deputy Chairman, Hammerson PLC

Andrew Popham Partner, PricewaterhouseCoopers

George Rose Finance Director, BAE SYSTEMS plc

Rosemary Thorne

Group Finance Director,
Bradford & Bingley plc

Tony Wedgwood

Formerly Technical Partner, KPMG

Secretary

Ann Wilks CBE

Assistant Secretary

Carol Page

In 2003 David Mitchell ceased to be a member of the FRRP.

APPENDIX 2

FINANCIAL INFORMATION

The statutory accounts of The Financial Reporting Council Limited and its subsidiaries, The Accounting Standards Board Limited and The Financial Reporting Review Panel Limited, are contained in its separately published Report and Financial Statements, copies of which are available free of charge on request. Statutory accounts for the year ended 31 March 2003 and the auditors' unqualified report thereon have been filed with the Registrar of Companies. The following information is only a partial extract and does not therefore represent those statutory accounts, reference to which should be made for a full understanding of the position.

(A) CONSOLIDATED INCOME AND EXPENDITURE*
- year to 31 March 2003

	Total £000
Contributions from sponsors (Note 1)	2,280
Gross income from publications	504
TOTAL INCOME	<u>2,784</u>
Operating charges:	
Staff costs	1,913
Other operating charges	879
Depreciation	5
Costs of Review Panel investigations	10
TOTAL OPERATING CHARGES (Note 2)	<u>2,807</u>
OPERATING DEFICIT	(23)
Interest receivable	92
SURPLUS BEFORE TAXATION	69
Taxation	<u>(15)</u>
SURPLUS FOR THE FINANCIAL YEAR	<u>54</u>

*Note: the movements in the legal costs fund during the year are shown in Note 3 below.

**(B) SUMMARISED GROUP BALANCE SHEET -
as at 31 March 2003**

	£000	£000
<i>Fixed assets</i>		
Office equipment, furniture and fixtures and fittings		43
<i>Current assets</i>		
Debtors	281	
Cash at bank		
General	379	
Legal Costs Fund	<u>2,002</u>	
		<u>2,662</u>
TOTAL ASSETS		2,705
<i>Current liabilities</i>		
Creditors		215
TOTAL ASSETS LESS CURRENT LIABILITIES		<u>2,490</u>
 CAPITAL AND RESERVES		
Accumulated Surplus		500
Legal Costs Fund (Note 3)		1,990
		<u>2,490</u>

(C) NOTES

1. Contributions were received from the following:

Accountancy profession
Consultative Committee of Accountancy Bodies

Government etc
Department of Trade and Industry
Department of Economic Development, Northern Ireland
National Audit Office

The City

Financial Services Authority
 Bank of England, on behalf of the banking sector
 Association of British Insurers
 National Association of Pension Funds
 Association of Investment Trust Companies
 Association of Unit Trusts and Investment Funds

2. Total operating charges were attributable as follows:

	£000
FRC	370
ASB	2,117
Review Panel	320
	<hr/>
	2,807

3. Legal Costs Fund

The Legal Costs Fund has been created to enable the Financial Reporting Review Panel to take steps to ensure compliance with the accounting requirements of the Companies Act 1985, including applicable accounting standards, and to investigate departures from those standards and requirements. Those funds may be used only for this purpose and may not be used to meet other costs incurred by the Group.

Movements in the Fund during the year were as follows:

	£000
Balance at 1 April 2002	1,990
Contributions from sponsors	10
Less cost of Review Panel investigations	(10)
	<hr/>
Balance at 31 March 2003	1,990

APPENDIX 3

ASB PUBLICATIONS

A: ASB PUBLICATIONS IN 2003

The Board issued the following publications in 2003:

Standard

Amendment to FRS 5 'Reporting the Substance of Transactions': Revenue Recognition (*November*)

Statement

Operating and Financial Review (*January*)

UITF Abstracts

Abstract 36 Contracts for sales of capacity
(*Information Sheet 58, March*)

Abstract 37 Purchases and sales of own shares
(*Information Sheet 64, October*)

Abstract 38 Accounting for ESOP trusts
(*Information Sheet 65, December*)

Abstract 17 (Revised 2003) Employee share schemes
(*Information Sheet 65, December*)

Exposure drafts

Amendment to FRS 5 'Reporting the Substance of Transactions': Revenue Recognition (*February*)

FRED 32 Disposal of Non-current Assets and Presentation of Discontinued Operations (*July*)

FRED 30 Supplement: Financial Instruments: Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk (*August*)

Proposed UITF Abstracts

Proposed Abstract on accounting for treasury shares
(*Information Sheet 59, May*)

Proposed revised Abstract 13 'Accounting for ESOP trusts'
(*Information Sheet 60, May*)

Proposed Abstract on accounting for emission rights
(*Information Sheet 61, May*)

Proposed Abstract on purchases and sales of own shares
(*Information Sheet 62, July*)

Proposed amendment to Abstract 17 'Employee share schemes'
(*Information Sheet 63, October*)

Consultation Papers

IASB Proposals on Insurance Contracts (*July*)

Discussion Paper

Statement of Principles for Financial Reporting: Proposed Interpretation
for Public Benefit Entities (*May*)

**B: STATEMENTS OF RECOMMENDED PRACTICE (SORPS):
DRAFTS AND FINAL TEXTS ISSUED IN 2003**

Title	Issuer	Date
Accounting and Reporting by Charities, Update Bulletin 1 (final)	Charity Commission for England and Wales	January
Financial Statements of Investment Trust Companies (revised) (final)	Association of Investment Trust Companies	January
Financial Statements of Authorised Funds (draft)	Investment Management Association (IMA)	May
Code of Practice on Local Authority Accounting in the United Kingdom 2003 (final)	The Chartered Institute of Public Finance and Accountancy	July
Accounting for Further and Higher Education (final)	Universities UK	October
Accounting for Insurance Business 2003 (final)	Association of British Insurers	November
Code of Practice on Local Authority Accounting in the United Kingdom 2004 (draft)	The Chartered Institute of Public Finance and Accountancy	November
Financial Statements of Authorised Funds (final)	Investment Management Association (IMA)	November

C: ASB PUBLICATIONS CURRENT AT 31 DECEMBER 2003
Accounting standards

(a) *Statements of Standard Accounting Practice (SSAPs) developed by the former Accounting Standards Committee or its predecessor and adopted by the Accounting Standards Board*

SSAP 4	Accounting for government grants
SSAP 5	Accounting for value added tax
SSAP 9	Stocks and long-term contracts
SSAP 13	Accounting for research and development
SSAP 17	Accounting for post balance sheet events
SSAP 19	Accounting for investment properties
SSAP 20	Foreign currency translation
SSAP 21	Accounting for leases and hire purchase contracts
SSAP 24	Accounting for pension costs <i>now being superseded by FRS 17</i>
SSAP 25	Segmental reporting

(b) *Financial Reporting Standards (FRSs) issued by the Accounting Standards Board*

FRS 1 (Revised 1996)	Cash Flow Statements
FRS 2	Accounting for Subsidiary Undertakings
FRS 3	Reporting Financial Performance
FRS 4	Capital Instruments
FRS 5	Reporting the Substance of Transactions
FRS 6	Acquisitions and Mergers
FRS 7	Fair Values in Acquisition Accounting
FRS 8	Related Party Disclosures
FRS 9	Associates and Joint Ventures
FRS 10	Goodwill and Intangible Assets
FRS 11	Impairment of Fixed Assets and Goodwill
FRS 12	Provisions, Contingent Liabilities and Contingent Assets
FRS 13	Derivatives and other Financial Instruments: Disclosures
FRS 14	Earnings per Share
FRS 15	Tangible Fixed Assets
FRS 16	Current Tax
FRS 17	Retirement Benefits
FRS 18	Accounting Policies
FRS 19	Deferred Tax
FRSSE	Financial Reporting Standard for Smaller Entities (effective June 2002)

(c) *Amendments to accounting standards*

Amendment to FRS 3 'Reporting Financial Performance':
Insurance Companies—June 1993

Amendment to SSAP 19 'Accounting for investment properties'—
July 1994

Amendment to FRS 5 'Reporting the Substance of Transactions':
Insurance Broking Transactions and Financial
Reinsurance— December 1994

Amendment to SSAP 21 'Accounting for leases and hire purchase
contracts': Tax-free Grants—February 1997

Amendment to FRS 5 'Reporting the Substance of Transactions':
Private Finance Initiative and Similar Contracts—
September 1998

Amendment to FRS 3 'Reporting Financial Performance':
Insurance Companies—June 1999

Amendment to FRS 17 'Retirement Benefits' and Financial
Reporting Standard for Smaller Entities (effective June 2002)
—November 2002

Amendment to FRS 5 'Reporting the Substance of Transactions':
Revenue Recognition—November 2003

Urgent Issues Task Force (UITF) pronouncements

- | | |
|------------------|---|
| UITF Abstract 4 | Presentation of long-term debtors in current assets |
| UITF Abstract 5 | Transfers from current assets to fixed assets |
| UITF Abstract 6 | Accounting for post-retirement benefits other than pensions <i>now being superseded by FRS 17</i> |
| UITF Abstract 9 | Accounting for operations in hyper-inflationary economies |
| UITF Abstract 11 | Capital instruments: issuer call options |
| UITF Abstract 13 | Accounting for ESOP trusts
<i>now being superseded by UITF Abstract 38</i> |
| UITF Abstract 15 | Disclosure of substantial acquisitions (revised 1999) |
| UITF Abstract 17 | Employee share schemes (revised 2000 and 2003) |
| UITF Abstract 18 | Pension costs following the 1997 tax changes in respect of dividend income
<i>now being superseded by FRS 17</i> |
| UITF Abstract 19 | Tax on gains and losses on foreign currency borrowings that hedge an investment in a foreign enterprise |

UITF Abstract 21	Accounting issues arising from the proposed introduction of the euro
UITF Abstract 21: Appendix	Further accounting issues arising from the introduction of the euro
UITF Abstract 22	The acquisition of a Lloyd's business
UITF Abstract 23	Application of the transitional rules in FRS 15
UITF Abstract 24	Accounting for start-up costs
UITF Abstract 25	National Insurance contributions on share option gains
UITF Abstract 26	Barter transactions for advertising
UITF Abstract 27	Revision to estimates of the useful economic life of goodwill and intangible assets
UITF Abstract 28	Operating lease incentives
UITF Abstract 29	Website development costs
UITF Abstract 30	Date of award to employees of shares or rights to shares
UITF Abstract 31	Exchanges of businesses or other non-monetary assets for an interest in a subsidiary, joint venture or associate
UITF Abstract 32	Employee benefit trusts and other intermediate payment arrangements
UITF Abstract 33	Obligations in capital instruments
UITF Abstract 34	Pre-contract costs
UITF Abstract 35	Death-in-service and incapacity benefits
UITF Abstract 36	Contracts for sale of capacity
UITF Abstract 37	Purchases and sales of own shares
UITF Abstract 38	Accounting for ESOP trusts

Other definitive statements

ASB Statement of Aims
Foreword to Accounting Standards
Foreword to UITF Abstracts
Operating and Financial Review (revised 2003)
Interim Reports
Preliminary Announcements
Statement of Principles for Financial Reporting
SORPs: Policy and Code of Practice

Financial Reporting Exposure Drafts (FREDs) and other exposure drafts

FRED 22	Revision of FRS 3 'Reporting Financial Performance'
FRED 23	Financial Instruments: Hedge Accounting
FRED 24	The Effects of Changes in Foreign Exchange Rates & Financial Reporting in Hyperinflationary Economies
FRED 25	Related Party Disclosures
FRED 26	Earnings per Share
FRED 27	Events After the Balance Sheet Date
FRED 28	Inventories & Construction and Service Contracts

FRED 29	Property, Plant and Equipment & Borrowing Costs
FRED 30	Financial Instruments: Disclosure and Presentation & Recognition and Measurement
FRED 30 Supplement	Financial Instruments: Fair Value Accounting for a Portfolio Hedge of Interest Rate Risk
FRED 31	Share-based Payment
FRED 32	Disposal of Non-current Assets and Presentation of Discontinued Operations

Discussion Papers

Derivatives and other Financial Instruments
(partly superseded by FRS 13)
Leases: Implementation of a New Approach
Review of the Financial Reporting Standard for Smaller Entities (FRSSE)
Statement of Principles for Financial Reporting:
Proposed Interpretation for Public Benefits Entities

Consultation Papers

Financial Instruments and Similar Items
IASB Proposals on Business Combinations, Impairment and Intangible Assets
IASB Proposals on Insurance Contracts

Working Paper

Discounting in Financial Reporting

Occasional papers *(produced jointly with other standard-setting bodies)*

- Future Events: A Conceptual Study of their Significance for Recognition and Measurement [1994]
- Major Issues related to Hedge Accounting [1995]
- International Review of Accounting Standards Specifying a Recoverable Amount Test for Long-lived Assets [1997]
- Reporting Interests in Joint Ventures and Similar Arrangements [1999]
- Accounting by Recipients for Non-Reciprocal Transfers, Excluding Contributions by Owners: Their Definition, Recognition and Measurement [2000]

Other publications

Liabilities and how to account for them: an exploratory essay, by Andrew Lennard.

The ASB publishes a quarterly newsletter 'Inside Track'. UITF announcements, including draft UITF Abstracts, are published in UITF Information Sheets. Press and UITF announcements are also available immediately on the ASB Website, which provides an automatic notification facility.

A comprehensive list of documents published by the ASB (and by the FRC and the FRRP) since 1990 can be downloaded from the Website (www.asb.org.uk). Details of how to obtain these publications are available on the Website.

APPENDIX 4

PROGRESS TOWARDS EU ADOPTED IFRS 2005 AT DECEMBER 2003

International Financial Reporting Standards

Work in progress towards 2005 deadline

IAS 7	Cash flow statements	Standards not forecast to change before March 2004. These were all adopted by the EU in September 2003.	
IAS 11	Construction contracts		
IAS 12	Income taxes		
IAS 14	Segment information		
IAS 18	Revenue recognition		
IAS 20	Government grants		
IAS 23	Borrowing costs		
IAS 29	Financial reporting in hyperinflationary economies		A number of these standards are, however, scheduled for reconsideration by the IASB after 2005.
IAS 30	Disclosures in the financial statements of banks and similar financial institutions		
IAS 34	Interim financial reporting		
IAS 37	Provisions, contingent liabilities and contingent assets		
IAS 41	Agriculture		
IFRS 1	First time adoption of IFRS	Issued June 2003 and awaiting EU adoption.	
IAS 1	Presentation of financial statements	Proposals for amendment issued in May (*December) 2002.	
IAS 2	Inventories		
IAS 8	Accounting policies, changes in accounting estimates and errors		
IAS 10	Events after the balance sheet date	Original standards adopted by the EU in September 2003.	
IAS 16	Property, plant and equipment		
IAS 17	Leases		
IAS 21	The effects of changes in foreign exchange rates		
IAS 24	Related party disclosures	Revised standards issued in December 2003 and awaiting EU adoption.	
IAS 27	Consolidated and separate financial statements		
IAS 28	Accounting for investments in associates		
IAS 31	Financial reporting of interests in joint ventures*		
IAS 33	Earnings per share		
IAS 40	Investment property		

IAS 32	Financial instruments: disclosure and presentation	Amendment proposals issued in June 2002 and August 2003. Revised text issued in December 2003, with amendments for macro-hedging changes expected in Q1 2004. Will then await EU adoption.
IAS 39	Financial instruments: recognition and measurement	
IAS 22	Business combinations	Amendment proposals issued in December 2002. Original standards adopted by EU in September 2003. Amended standards due for issue in Q1 2004 and will then await EU adoption.
IAS 36	Impairment of assets	
IAS 38	Intangible assets	
IAS 35	Discontinuing operations	Amendment proposals issued in July 2003. Original standard adopted by EU in September 2003. Revised standard due for issue in Q1 2004 and will then await EU adoption.
IAS 19	Employee benefits	Standard adopted by EU in September 2003. May be amended for 2006 (and for early adoption in 2005?) but amendments will need rapid progress and EU adoption.
IFRS [2]	Share-based payment	Proposals issued in November 2002. Standard due for issue Q1 2004 and will then await EU adoption.
IFRS [3]	Insurance	Proposals issued in July 2003. Standard due for issue in Q1 2004 and will then await EU adoption.

APPENDIX 5

FINANCIAL REPORTING REVIEW PANEL PRESS NOTICES ISSUED IN 2003

<i>FRRP PN number</i>	<i>Date of issue</i>	<i>Company</i>	<i>Matter in question</i>
75	31 January	Finelot plc	Treatment of start-up costs
76	14 February	Kensington Group plc	Presentation of quasi- subsidiaries in consolidated accounts

FRRP Press Notices can be downloaded from the Website (www.frrp.org.uk)

APPENDIX 6

FINANCIAL REPORTING COUNCIL ACCOUNTING STANDARDS BOARD FINANCIAL REPORTING REVIEW PANEL

STAFF AT 31 DECEMBER 2003

Staff serve on all three bodies—the FRC, the ASB (and its committees) and the Review Panel—as their responsibilities dictate.

Technical staff

Andrew Lennard	Director of Operations <i>up to 31 December 2003</i>
Jenny Carter*	Project Director
Janie Crichton	Project Director
Paul Ebling	Project Director
Hans Nailor	Project Director
Carol Page	Assistant Secretary to the Review Panel
Simon Peerless	Project Director
Duncan Russell*	Project Director

Administrative staff

Ann Wilks	Secretary to the FRC and the Review Panel
Charles Bridge*	Secretary to the ASB and the UITF Assistant Secretary to the FRC

Secretarial staff

Lisa Cattanach	Secretary to Andrew Lennard and others
Alison Chambers	IT Manager and Secretary to Allan Cook
Alison Cooper	Secretary to Ann Wilks and others
Carol Liuzzi	Secretary to Sir Bryan Nicholson, Charles Bridge and others
Erica Taylor	Secretary to Mary Keegan

**On secondment to the FRC*