

**Minutes of the meeting of the Accounting Council of the FRC on 10 April 2014 at
Aldwych House, 71-91 Aldwych, London, WC2B 4HN**

Present:

Roger Marshall	Chair
Richard Barker	Council Member
Anne McGeachin	Council Member
Gunnar Miller	Council Member
Liz Murrall	Council Member
Veronica Poole	Council Member
Pauline Wallace	Council Member

Observers:

Mike Ashley	EFRAG Observer
Alison Ring	HMRC observer
Michael Kavanagh	IAASA Observer
Phillip Trotter	HMT Observer

In attendance:

Anthony Appleton	Director of Accounting and Reporting
Jenny Carter	Director of UK Accounting Standards, Accounting & Reporting Policy Team
Francesca Chittenden	Council Secretary
Roz Clarke	Project Manager, Accounting & Reporting Policy Team
Annette Davis	Project Director, Accounting & Reporting Policy Team
Jennifer Guest	Project Director, Accounting & Reporting Policy Team
Andrew Lennard	Director of Research
Melanie McLaren	Executive Director
Susanne Pust Shah	Project Director, Accounting & Reporting Policy Team
Deepa Raval	Project Director, Accounting & Reporting Policy Team
Andrea Jeffries	Building Societies Association (BSA) – minute 8 only
Andrew Payton	Hinckley & Rugby Building Society – minute 8 only
Neal Walker	Marsden Building Society – minute 8 only

Apologies

Apologies were noted from Chris Buckley and Ken Lever (Council Members).

The Council noted that Anne McGeachin would be taking on a role at the IASB in May and, accordingly, Anne had tendered her resignation from the Council and that the meeting would be her last. The Chairman placed on record his thanks to Anne for her contributions to the work of the Council.

The Chairman also placed on record his thanks to Ken Lever, who was unable to attend the meeting, for his contributions to the work of the Council.

1. Minutes of the Previous meeting and rolling actions

- 1.1 The minutes of the previous meeting were approved for publication subject to the replacement of the word 'implementation' with 'undertaking' at paragraph 3.4.
- 1.2 The rolling action log was noted.

2. Director of Accounting Report

- 2.1 The Council noted a paper which provided an update on developments relating to UK and international accounting standards, matters of policy and an over view of staff activities during March – April 2014. Particular attention was given to the following matters:

International developments

- 2.2 The Council noted that the IASB had begun its public consultation stage of its post-implementation review of IFRS 3 by publishing a Request for Information. The Council noted that a joint EFRAG and European Standards Setters questionnaire had been developed to draw out the important issues of the IFRS 3 review and was available on the FRC website; Members were invited to submit comments on the questionnaire to FRC staff. The Council also noted a summary of the key points raised at a joint FRC / ICAEW IFRS 3 Business Combinations RFI outreach event and that those points would be incorporated in to a draft response which would be shared with the Council at its next meeting.
- 2.3 The Council also noted that the IASB was progressing its work on insurance contracts and on leases and noted the latest 'thinking' in relation to those projects.

European Developments

- 2.4 The Council noted the following:
 - The Accounting Regulatory Committee (ARC) had met on 8 April and had received a presentation from Mr Maystadt on EFRAG reform; whilst there was general agreement and support for the proposals there remained some concern in relation to private sector versus public sector representation on the EFRAG board.
 - EFRAG had issued a paper on long term financing which is a major area for initiatives in Europe. Accounting topics that might be subject to further analysis included the impact, if any, of the use of fair value accounting on short-term decision making, the use of simplified accounting standards for SME listed companies and the introduction of a European accounting standard for SME unlisted companies.
 - The European Commission (EC) was in the process of establishing an expert group, including academics, users and preparers and representatives of Civil Society groups and public bodies, to assist the EC in developing a questionnaire, and analysing the results of that questionnaire, to assess the effects of using IFRS in the EU.

- Initial discussions on the endorsement of IFRS 14 highlighted a significant level of antipathy amongst Member States. It is currently unclear how many companies in Europe could fall within its scope, but the expectation is that its application would be very limited if endorsed.
- The FRC had submitted a comment letter to the European Banking Authority (EBA) on its consultation relating to guidelines on disclosure of encumbered and unencumbered assets. The response highlighted the FRC's concerns that the guidelines will create conflict between regulatory requirements and disclosures required by IFRS.

UK Developments

2.5 The Council noted the following:

- Discussions were taking place in relation to the development of a joint or parallel consultation with BIS to consider the Member State options in response to the EU Accounting Directive.
- Work to develop proposed Financial Reporting Standards for Micro-Entities (FRSME) was continuing but that without details of the changes to company law, this work, and work to progress potential amendments to existing accounting standards is limited.
- The UK GAAP Technical Advisory Group had met and discussed the pros and cons of introducing accounting consistent with IFRIC 14 into UK GAAP. A paper will be brought to the Council in May.

Council Effectiveness

2.6 The Council considered a range of administrative matters regarding Council meetings. The Council agreed that moving forward Council meetings should continue to be held on Thursday mornings. It was also agreed that the Council's away day should be held on 17 July so that the Council's input can be fed in to the FRC Board's deliberations at its strategy day in September.

3. Director of Research

3.1 Andrew Lennard (AL) introduced a paper that set out a brief overview of current accounting research activities. The Council noted:

- That Bulletins on measurement, OCI and recycling were in development and would be brought to the Council for consideration in May;
- A summary of the key discussion points made at a meeting of EFRAG's Planning & Policy Committee on 19 March;
- A summary of the issues considered by the Academic Panel at its meeting on 14 March;
- A draft research paper entitled 'Research on the statement of Cash Flows: taking stock'. AL invited Council Members to submit comments on the research paper by email.

3.2 The Council noted that IASB had considered summaries of the comment letters received on the Discussion paper 'A review of the Conceptual Framework' at its March meeting. The Council noted that whilst many respondents had expressed similar views to the views set out in the FRC response, there were a small number of points on

which respondents had expressed different views, specifically that many do not see a need to make major changes in the definitions of income and expenses, and that many agreed with the proposal to retain the existing discussion of capital maintenance concepts.

- 3.3 AL introduced a note that he and the Chairman had developed to inform discussion with IASB staff and members, and certain investors, on prudence and how it could be reflected, and potentially reintroduced, to the Conceptual Framework. The Council welcomed the note and the discussion relating to the issues of recognition asymmetry, measurement and prudence and neutrality. The Council suggested that further consideration should be given to the relationship between prudence and reliability. The Council also suggested that the section relating to financial services should be reviewed so that industry is not seen as an 'exception' to the rule. In response to the suggestion that a definition of prudence was needed AL clarified the note was intended to assist the IASB and others in reaching agreement on the concept of prudence and that once this agreement had been reached, work to define that concept would follow. The Council highlighted that reintroducing prudence to the Conceptual Framework should be in tandem with the reintroduction of the concept of stewardship. The Council also highlighted the importance of defining who the accounts are for.
- 3.4 AL informed the Council that the IASB had begun its reconsideration of leases and had made a number of decisions, a number of which are consistent with some of the views expressed during the FRC's outreach activities. The Council noted that no decision had yet been taken on the suggestion that the provision of services should be out of the scope of the standard. The FRC had discussed the issue with IASB staff, IASB Member Darrell Scott, the FASB and other European Standard Setters, the latter of whom held views closely aligned with those of the FRC. The Council noted that the IASB was due to discuss the issue at its next meeting and that an update would be provided to the Council in due course.

4. Horizon scanning

- 4.1 The Council suggested that there may be a number of accounting related issues to consider in response to the changes being proposed by the HMT with regards to pensions, particularly, the accounting treatment of bulk annuities. It was noted that the Actuarial Council would be contributing to the development of an FRC response to the HMT consultation 'Freedom and choice in pensions' and it was suggested that that the Accounting Council should also feed in to the development of that FRC response.

5. Draft SORP: PRAG (Pension Schemes)

- 5.1 Jennifer Guest (JG) introduced the draft PRAG SORP for Financial Reports of Pension Schemes for comment.
- 5.2 The Council noted the approach taken to the draft and the summary of changes that had been made from the 2007 version. JG highlighted that, in accordance with legislation, the draft SORP permits annuities to be reported at Nil value; which is inconsistent with FRS 102 which requires annuities to be valued. The Council noted

that the discrepancy had been debated thoroughly during the initial consultation process and that a statement had been inserted to FRS 102 to confirm the legal provision. The Council noted that whilst the FRC Statement, which would accompany the final SORP, would confirm that the SORP is consistent with accounting standards, the statement should be revised to highlight that the balance sheet excludes pensions liabilities. The Council requested that this statement also be issued with the exposure draft.

- 5.3 The Council discussed whether the investment transaction cost disclosures requirements in the draft PRAG SORP could be considered inconsistent with the requirements set out in the Investment Management Association (IMA) SORP. The Council suggested that the PRAG SORP working party consider reviewing the disclosure requirements listed at paragraph 3.8.42 to reflect the same level of granularity of the disclosure of charges as is in the IMA SORP.
- 5.4 Subject to the amendments detailed above the Council approved the draft SORP for issue by the PRAG for consultation as an ED. The Council noted that the PRAG SORP working party intend to publish the ED as soon as possible.

6. SORP: Charity Commission and OCSR (Charities)

- 6.1 Jenny Carter (JC) introduced the final draft of the FRS 102 Charity SORP and the FRSSE Charity SORP for consideration and recommendation to the FRC Board and Committees. JC praised the proactive approach the SORP-making body had taken in encouraging engagement from stakeholders and the careful consideration the SORP-making body had given to the range of views expressed.
- 6.2 The Council noted that, in response to consultation feedback, the SORP-making body had decoupled the FRSSE and FRS 102 requirements with the intention of issuing separate SORPs for the two accounting regimes. The Council queried whether respondents had been made suitably aware when responding to the consultation question that, if a FRSSE SORP were to be developed, it would only have a shelf life of one year. The Council suggested that this point may not have been sufficiently highlighted in the consultation, and that it might be disproportionate to require small charities with limited resources to appear to have to change their accounting practice twice in a two year period. Accordingly, the Council asked for more information, and was provided with it, on alternatives considered by the SORP-making body and suggested that the SORP making body consider its communication strategy around the new FRSSE SORP and the extent of change it will introduce, given its short shelf life.
- 6.3 The Council noted the varying views expressed by the FRC's Committee on Accounting for Public Benefit Entities (CAPE) and the SORP making bodies in relation to Multi-columnar Statement of Financial Activities (SOFA) and presentation of comparative information. The Council agreed that the SORP should be transparent and explicitly allow a free choice between presenting comparative information either on the face of the SOFA or in a prominent note.

6.4 The Council also agreed with the approach for accounting for legacy income and the approach to disclosures around senior staff remuneration. However, the Council highlighted that the disclosure requirements for trustee remuneration are greater than the requirements of the education SORPs and suggested that this inconsistency should be fed back to the SORP making bodies.

7. SORP: Housing Federations (Social Housing Providers) – Narrow-scope exposure draft on impairments

7.1 JC introduced the final draft of the narrow-scope exposure draft (ED) on impairments, in the Housing SORP. JC clarified that the narrow-scope ED had been developed in response to requests to review the requirements set out in the original ED with respect to impairments of housing properties.

7.2 The Council endorsed the approach set out in the narrow-scope ED, namely, that ,whilst the sector is largely cash flow driven, properties are held for social benefit, and social landlords should be permitted to measure social housing properties based on their service potential and that depreciated replacement cost is an appropriate measure for determining value in use.

7.3 The Council approved the ED and consultation questions for issue, the Council also endorsed the proposal that the consultation be open for an eight-week period, as opposed to the usual three months, given the narrow-scope. The Council highlighted the importance of the SORP making body performing focussed outreach to encourage investors and lenders to respond to the consultation.

8. FRED 51: Hedge Accounting – discussion with BSA representatives

8.1 The Chairman welcomed Andrea Jeffries (AJ), Andrew Payton and Neal Walker as guests to the meeting. The Chairman invited them to discuss with the Council how building societies hedge interest rate risk in mortgage portfolios, and the proposed accounting for such hedges. The dialogue was initiated by the Council to inform its deliberations as to whether the Council should revise its previous advice to the FRC Board, contained in FRED 51 *Hedge Accounting*, that macro-hedging provisions should not be included in FRS 102.

8.2 AJ thanked the Council for the opportunity to clarify the concerns that had been expressed by the Building Societies Association (BSA) in response to FRED 51.

8.3 NW summarised the practical issues societies face when applying hedge accounting. NW explained that societies enter into interest rate swaps (fixed to floating) to hedge the interest rate exposure in a pool of fixed rate mortgages. NW highlighted that societies are under the law restricted to use derivatives for the purpose of hedging risk and, accordingly, an economic relationship between the hedged item and the hedging instrument must exist. NW noted that the macro-hedge provisions in IAS 39 are more suited to entities with large portfolios of mortgages, rather than for smaller building societies with a relatively small loanbook. He explained that mortgages are subject to prepayment and as and when mortgages are prepaid prior to the expected repayment date new mortgages are added to a portfolio to ensure the value of the swap continues

to be matched with the value of the hedged mortgage portfolio.

- 8.4 Through discussion the following observations and points of clarification were made:
- Societies hedge gross positions, i.e. a pool of mortgages, rather than net positions, e.g. the net of mortgages and deposits;
 - Because of the small number of mortgages in a pool that is designated as a hedged item, the unexpected prepayment of one mortgage can affect the effectiveness of a hedge disproportionately compared to a large pool of mortgages where prepayment of one mortgage is relatively inconsequential for the overall effectiveness of the hedge;
- The replacement mortgages in the mortgage pool could be on significantly different terms and in some instances may no longer match with the critical terms of the swap, which may create greater ineffectiveness going forward
- 8.5 The Council noted that the introduction of macro-hedging provisions in FRS 102 may not resolve the problems identified by the BSA when applying the macro-hedging provisions in IAS 39. It was noted that a worked example that demonstrates how macro-hedging is applied would aid in forming a final view on the issue.
- 8.6 The Council and BSA representatives also discussed concerns held by the BSA in relation to the application of the effective interest rate method and impairment requirements in FRS 102.
- 8.7 The Chairman concluded the discussion and noted that the issues raised will be debated again at the next meeting in May with a view to clarifying the position of the Council and its advice to the FRC Board.

9. Guidance on the Strategic Report

- 9.1 Deepa Raval (DR) introduced a complete draft of the 'Guidance on the Strategic Report' including the 'Basis for Conclusions' and a cover paper summarising the main changes that had been made to the draft Guidance from the ED. The Council noted that following discussion with the working group further changes would be made to the structure of the placement section of the guidance.
- 9.2 DR highlighted that the area that had changed the most since the ED was the 'placement' section, those changes included the removal of the terms 'core' and 'supplementary' from the guidance, and the addition of guidance on differentiating between 'sign posting' and 'cross referencing'. DR also highlighted that the original definition of 'materiality' had been retained in order to be consistent with accounting standards.
- 9.3 The Council noted that before publication the guidance would be amended to align the legal summaries with the final letter from BIS and align the wording on going concern disclosures with the output of the FRC's consultation 'Risk Management, Internal Control and the Going Concern Basis of Accounting'. The feedback statement to accompany the guidance would also be finalised.

9.4 The Council approved the draft guidance and noted that the guidance would be published in June. The Council congratulated DR and the team on their work in developing the guidance.

10. Alternative Performance Measures – ESMA Consultation

10.1 DR introduced a paper that provided an overview of the ESMA consultation paper (CP) 'ESMA Guidelines on Alternative Performance Measures' and a draft FRC response to the CP.

10.2 DR summarised a number of issues and concerns that had been identified by FRC staff in relation to the CP as follows:

- the concern around the enforceability of the guidelines, noting that the FRC's Conduct Committee does not have the powers over issuers;
- the broad scope of the CP which states that the draft guidelines would apply to "APMs disclosed by issuers in all documents containing regulated information that are publicly available";
- the broad definition of an APM – which is defined in the CP as "any numerical measure of historical, current or future financial performance, which relates to the financial position, comprehensive income or cash flows, other than a measure defined by the applicable financial reporting framework";
- a question over how the guidelines will interact with current requirements for reporting key performance indicators in UK law; and
- the potential overlap between the CP and proposals currently being developed by the IASB as part of its disclosure framework, in particular that the ESMA proposals in relation to APMs in the financial statements could be seen to be interpreting IFRS.

10.3 The Council acknowledged the concerns and supported the recommendation that the FRC should not support the CP. However, the Council suggested that the draft response letter should be revised to make clear the reasons why the FRC would be unable to adopt the measures set out. The Council also suggested that the FRC might want to encourage ESMA to publish the high level principles as guidelines, rather than as rules.

10.4 The Council noted EFRAG's response letter to the CP and supported the FRC's draft response letter to EFRAG.

11. Any other business

11.1 There was no other business.

12. Next meeting

12.1 The next meeting of the Accounting Council will be on 15 May 2014.