Minutes of a meeting of the Accounting Council held on Thursday 4 June 2015 in the Boardroom at 8th Floor, 125 London Wall, London, EC2Y 5AS

Present:

Roger Marshall	Chairman (ceded Chair for agenda item 5)
Richard Barker	Council Member
Chris Buckley	Council Member
Michael Gallagher	Council Member
Liz Murrall	Council Member
Mark Smith	Council Member
Jeremy Townsend	Council Member
Pauline Wallace	Council Member (Chair for agenda item 5)

Observers:

Matt Blake	HMRC Observer
Michael Kavanagh	IAASA Observer
Lee Piller	FCA Observer

In attendance:

Anthony Appleton	Director of Accounting and Reporting Policy
Francesca Carter	Council Secretary
Jenny Carter	Director of UK Accounting Standards, Accounting & Reporting
Annette Davis	Project Director, Accounting & Reporting Policy Team
Andrew Lennard	Director of Research
Seema Jamil-O'Neill	Project Director, Accounting & Reporting Policy Team
Melanie McLaren	Executive Director, Codes & Standards
Susanne Pust Shah	Project Director, Accounting & Reporting Policy Team
Deepa Raval	Project Director, Accounting & Reporting Policy Team
Roz Szentpéteri	Project Manager, Financial Reporting Council

Welcome and Apologies for absence

Apologies were noted from Gunnar Miller, Veronica Poole (Council Members) and Ross Campbell (HMT Observer)

1. Minutes of the previous meeting and rolling actions

1.1 The minutes of the meeting held on 14 May were approved for publication subject to a minor amendment at paragraph 4.3.

1.2 The Council reviewed and noted the rolling action log. AA reported that, due to timing constraints, it is unlikely that the Council will have the opportunity to review the IASB's governance arrangements in advance of the IASB's own review.

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 overview of staff activities since the last meeting. Particular attention was given to the following matters:

European Developments

2.2 The Council noted that, due to ill health, Mr Wolf Kinz had decided not to accept the EFRAG presidency and that Roger Marshall would continue in his interim role whilst a replacement is sought.

Accounting Regulatory Committee (ARC)

2.3 The Council noted that the ARC had met on 21 May and debated EFRAG's draft endorsement advice (DEA) on IFRS 9 Financial Instruments. AA reported that whilst Member States are generally supportive of the DEA there is still some concern with respect to the deferral of IFRS 9 for insurance companies.

EFRAG

2.4 The Council approved the completed Invitation to Comment (ITC) on *Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10, IFRS 12 and IAS 28)* for submission to EFRAG.

UK GAAP

2.5 The Council supported the proposal that, as part of the triennial review of FRS 102, consideration should be given to the intention of FRS 102 in areas where company law may restrict the use of fair value accounting for certain financial instruments and whether this should apply to all entities.

2.6 The Council noted that the Charity SORP-making body had considered the Council's advice and had decided not to proceed with the proposed Charities SORP (*FRS 102) Small entities*. Jenny Carter (JC) reported that the SORP-making body will propose a return to a single SORP for all charities which would include an option for charities not meeting the SORPs 'larger charities' definition to omit the cash flow statement. The Council welcomed the decision and requested the opportunity to comment on the revised ITC before it is issued.

IASB's Disclosure Initiative

2.7 AA reported on progress with the IASB's Disclosure Initiative. The Council noted that the executive consider there to be an increasing risk of further fragmentation of the Initiative and that the fragmented approach of issuing narrow scope amendments makes it difficult to assess the impact of those amendments in the round and results in the deferral of consideration of the more substantive issues. AA reported that the executive is considering writing to the IASB to express this concern and that a draft letter would be brought to the Council for consideration in due course.

3. Director of Research Report

3.1 Andrew Lennard (AL) introduced a report that provided an update on current accounting research activities. Particular attention was given to the following matters:

IASB Conceptual Framework

3.2 The Council noted that the IASB's ED of its Conceptual Framework (CF) had been published on 28 May with a 150 day comment period. AL reported that whilst the ED contains no surprises and does appear to reflect the views expressed by the FRC in responding to the Discussion Paper, there are some areas the FRC will wish to influence further.

3.3 AL summarised the areas he considered to be of most significance to the FRC. It was noted that, in several respects, the proposals in the Exposure Draft were consistent with the views expressed in the FRC response, and accordingly it would be appropriate for the FRC response to the ED to welcome them. Through discussion the following observations were made and advice was given:

3.4 *Stewardship*

- It was noted that whilst the ED places more emphasis on stewardship, stewardship is set within an overall objective of decision-usefulness and could fall short of the vision of providing information that is rich enough to enable investors to challenge management's strategies. One possibility is to explicitly broaden the scope of the decision-usefulness objective to embrace more than buy/hold/sell decisions.
- It was also noted that the approach to stewardship as set out in the ED might be strengthened by bringing in some of the wording from the IASB's new mission statement.
- The Council suggested that the FRC should seek to encourage the IASB to reconsider its approach in this area.

Prudence

- It was noted that whilst the IASB's thinking in respect of prudence has become more aligned with the FRC's thinking, there is a lack of discussion of the role of prudence in developing accounting policies that provide asymmetry. The Council suggested that the IASB should be encouraged to reconsider this approach.

Reliability

- It was noted that, despite encouragement from the FRC, the IASB has not decided to reinstate reliability and that the IASB intends to clarify that measurement uncertainty is one factor that can make financial statements less relevant.
- The Council supported the view expressed by AL that reliability is a useful concept in standard-setting and advised that the FRC should seek to influence the IASB's thinking in this area whilst having regard to any changes in the discussion of faithful representation.

Faithful representation

- It was noted that the IASB intend to include in the discussion of faithful representation that it requires that the substance and not merely the legal form of a transaction is reflected.

Performance measurement

- The main differences between the proposals and the view taken by the FRC in respect of performance measurement were noted and the Council advised that the FRC should seek to encourage the IASB to review their thinking in this area.

Presentation and Disclosure

- It was noted that it is unclear what aspects of presentation, other than the distinction between profit and loss and 'OCI', are likely to fall within the scope of the CF and what aspects will be considered as part of the Performance Reporting project.

3.5 The Council discussed the proposed timetable for consideration of the various issues listed above. It was suggested that consideration of ‘Profit & Loss and OCI’ be brought forward and that consideration of the approach to the business model be considered at the same time as Stewardship. AL undertook to revise the timetable.

3.6 The Council noted the agenda for the July meeting of the Accounting Standards Advisory Forum (ASAF).

4. Final Draft Amendments / Standards – FREDS 58, 59 and 60

4.1 JC introduced proposed draft amendments to FRS 100, FRS 101 – *2014/15 cycle and other minor amendments*, FRS 102 – *Small entities and other minor amendments*, and FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*. JC reported that the Impact Assessment and Feedback Statement would be presented to the Council for discussion at the 16 June Conference Call.

4.2 JC invited the Council to consider the draft amendments and to confirm its advice, subject to any issues discussed at the meeting or at the 16 June Conference Call, to the FRC Board to be issued. The Council noted that the amendments had been drafted to reflect the advice given by the Council at the April and May meetings.

Amendments to FRS 100

4.3 JC summarised the proposed drafting amendments to FRS 100. The Council noted that, as advised by the Council, paragraph AG10 had been revised to address an issue raised in respect of intra-group balances. Whilst the Council agreed with the principle that a disclosure exemption should be permitted in relation to intra-group balances, the Council suggested that the drafting be revised to improve clarity. The Council also suggested that paragraph 14 of the Accounting Council’s advice should be amended to clarify that preparers must adopt all of the amended standards in one go and that users can not apply one of the amended standards and not the others.

4.4 Subject to the drafting amendments set out at paragraph 4.3 the Council approved its advice to the FRC Board for the amendments to be issued.

Amendments to FRS 101

4.5 JC introduced the proposed amendments to FRS 101 and reported that some significant drafting amendments had been made. The Council discussed the proposed amendments and the following comments were made and advice was given:

- It was noted that the table at paragraph 11 of the Accounting Council’s advice would need to be updated to reflect the new timings of the endorsement of IFRS 15 and suggested that it would be helpful to set out that amendments to FRS 101 in response to the introduction of IFRS 15 would be considered as part of the next annual review.
- The Council noted that a paragraph had been inserted at paragraph 12 to clarify the effective dates of the amendments but questioned whether the drafting of the paragraph makes it sufficiently clear which provision need to be applied and when. The Council suggested that consideration should be given to listing the amendments arising from the 2014/15 cycle within the document and then inserting a cross reference to the rest of the amendments.

- It was suggested that paragraph 30 of the Council's Advice should be amended to clarify that in respect of *IFRS 3 Business Combinations* – Contingent consideration, FRED 57 proposes an amendment to the Application Guidance to 'ensure the underlying text from IFRS 3 is correct'.
- The Council noted that in drafting FRS 101 less emphasis is placed on the requirements of the Companies Act and that, rather than making reference throughout the standard to the Companies Act requirements as is done in FRS 102, it is made clear in the standard that users must take responsibility for ensuring they meet the requirements of company law in addition to the requirements of FRS 101. The Council discussed this approach and suggested that there may be some instances where special circumstances apply and it would be helpful to provide clarification within the body of FRS 101. On this basis the Council requested that clarification of the legal requirements in respect of the seriously prejudicial disclosure exemption in IAS 37 should be inserted in to FRS 101 to assist users, particularly those who are familiar with the IFRS by amending the application guidance as necessary.

4.6 Subject to the amendments discussed, the Council approved its advice to the FRC Board for the amendments to be issued.

Amendments to FRS 102

4.7 JC summarised the key proposed amendments to FRS 102. The Council noted that whilst the principles exposed in FRED 59 remain the same, significant drafting amendments had been made to improve the usability of the standard. JC reported that an early draft of the revised amendments to Section 1A *Small Entities* had been considered, and was supported by the UK GAAP Technical Advisory Group.

4.8 Through discussion of the proposed amendments the following observations were made and advice was given:

- The Council noted that Section 1A is drafted using the language of company law and promotes the need to give a 'true and fair view' which is different to the language used in Section 3, which refers to 'fair presentation'. The Council highlighted a need for the language used throughout the standard to be consistent and to be aligned with the language of company law. Accordingly the Council advised that Section 3 should be amended to be consistent with company law.
- It was commented that FRS 102 encourages users to consider the use of a true and fair override on a small number of occasions and that this is inconsistent with text set out at paragraph 1.AC10 of Appendix C to Section 1 which notes that the use of a true and fair override is only expected to occur in extremely rare circumstances. JC undertook to consider the possibility of amending the text at paragraph 1.AC10 as suggested but highlighted that as the text had been taken directly from Section 3 of FRS 102 and so there may be some 'knock on' effects to amend that text also.
- The Council noted a number of amendments to the Appendix IV: Note on legal requirements. JC highlighted that it had been clarified that for subsidiaries excluded from consolidation and measured at fair value through profit and loss, the true and fair override may not be necessary in relation to consolidated financial statements if that accounting would have been permitted by IFRS 10.
- JC reported that paragraphs 11.39 and 11.48A had been amended to note that the disclosures relate to financial instruments and not just financial liabilities. Whilst the Council noted that the solution avoids the existing problems that arise with

incorrectly paraphrasing the circumstances in which the additional disclosures apply, the solution is less user-friendly and increases the need for entities to refer directly to the Regulations. Following a brief discussion, and an acknowledgement that a very small sub-set of financial instruments would fall within the scope, the Council concluded that the solution is the most appropriate.

- The Council noted the revised drafting in respect of inventories held for distribution at no or nominal consideration. Through discussion it was suggested that the term 'distribution' may be confusing, whilst it was noted that the term is defined in the glossary it was suggested that, as part of the triennial review, consideration could be given to whether a different term could be used.
- AA reported that, following receipt of the comment letters, changes will be necessary to the amendments relating to the accounting for share-based payments. The approach set out in FRED 61 addresses the narrow issue that had been brought to the FRC's attention, but in relation to other situations with uncertain settlement outcomes the proposed solution is too simplistic and does not address all of the nuances of the broader and more contentious issues associated with share-based payments. The Council noted that the executive would re-consider the approach to addressing the broader, more contentious issues and would report to the Council at the 16 June conference call.
- The Council noted that the change in legislation to prohibit the reversal of impairment losses relating to goodwill is yet to be made.
- The Council discussed its advice with respect to Residents' Management Companies (RMCs) and agreed to return to the issue during the conference call on 16 June 2015.
- The Council suggested that the references to fair presentation as set out at paragraph 1A.17 should be strengthened.
- The Council noted that the changes in the law that are to be made for the Accounting Directive will not apply to LLPs and that it is expected that an equivalent change would be made to relevant LLP accounting. The Council noted that text to highlight the differences between the two sets of legislation would be inserted in to the *Note on Legal Requirements*.

4.9 The Council noted that the Amendments to FRS 102 and the Council's Advice would be updated to reflect the views expressed by the Council and circulated for consideration by the Council on 16 June.

FRS 105

4.10 Susanne Pust-Shah (SPS) introduced the proposed FRS 105. The Council noted that the standard had been updated to reflect the views expressed by the Council at the May meeting and to reflect evidence that had been gathered in respect of the accounting for government grants. The Council agreed with the amendments made.

4.11 SPS invited the Council to comment on the proposals, the following observations were made and advice was given:

- The Council noted that, as discussed at the May meeting, the scope had been widened to permit unincorporated businesses to apply FRS 105 where appropriate and to allow micro-entities to include additional information to that required under the law provided they are produced applying relevant standards.

- The Council supported the proposal to make the standard as user-friendly and accessible as possible and requested that the empty sections of the standard should be removed and that the numbers of the remaining sections should run sequentially.
- The Council noted that Sections 11 and 12 have been merged and that the new Section 11 covers the accounting for all financial instruments. It was also noted that consideration is being given to merging Section 16 *Investment Property* with Section 17 *Property, Plant and Equipment*.

4.12 The Council noted that a revised FRS 105 would be presented to the Council at the 16 June conference call.

5. IFRS 9 'Financial Instruments' – Draft endorsement advise

5.1 Seema Jamil'O'Neill (SJON) introduced a proposed response to EFRAG's invitation to comment on the DEA and an analysis of EFRAG's assessment of whether IFRS 9 *Financial Instruments* meets the technical endorsement criteria and is conducive to the public good. SJON reminded the Council that it had considered EFRAG's assessment of the main changes introduced by IFRS 9 and the technical endorsement criteria at its May meeting. SJON noted that the views expressed by the Council at the previous meeting had been reflected in the draft FRC response.

Prudence

5.2 SJON reported that whilst the FRC consider there to be two aspects of prudence: (i) the exercise of caution when making judgements under conditions of uncertainty and (ii) the more timely recognition of losses than of gains ('asymmetry in recognition'), the executive agree with EFRAG's initial assessment that IFRS9 leads to prudent accounting. SJON also reported that the executive also consider that there is no need for a direct reference to asymmetry in recognition on the basis that this is addressed in the IFRS 9 requirement for impairment of assets classified and measured at amortised cost. The Council supported the executive view but noted that, as a concept, the impairment model itself is not prudent but that the application of the impairment model results in prudence.

Conducive to European Public good

5.3 SJON reported that EFRAG had considered a number of issues in determining whether IFRS 9 could be considered conducive to European Public good. EFRAG had concluded that overall IFRS 9 is a clear improvement over IAS 39, with the exception of classification and the measurement of financial assets. SJON reported that EFRAG had identified potential negative impacts that the IFRS 9 requirements may have on investor and issuer behaviour but had concluded that it is unable to determine whether those impacts would materialise.

5.4 The Council noted and discussed the issues raised by EFRAG in respect of classification and measurement requirements in detail and agreed that whilst IFRS 9 is an improvement on IAS 39 there are a number of issues that require further exploration. Accordingly the Council advised that the response to question 5 of the DEA should state that the FRC agrees with EFRAG's initial assessment, .although, in relation to the treatment of equity investments and the non-separation of embedded derivatives from the host financial asset, it should reflect the balancing arguments that led to the development of IFRS 9 in the first place. The Council also advised that the FRC should further explore evidence as to whether financial instruments held as measured at amortised cost or classified as AFS under IAS 39 would meet the IFRS 9 SPPI test and that the response should not make reference to the issue until further exploration has taken place.

5.5 The Council noted the potential negative impacts of IFRS 9 requirements on investor and issuer behaviour identified in the EFRAG DEA and that the FRC has seen no evidence in the UK to suggest the impacts would occur. Through discussion the Council advised that the response should be redrafted to be more positive in tone, setting out the FRC does not have any evidence to suggest that the impacts identified by EFRAG may occur and request that the EFRAG DEA assessment should highlight some of the mitigating information it already has on these issues.

Interrelationship with IFRS 4 Phase II

5.6 The Council noted that EFRAG has identified the interrelationship with IFRS 4 Phase II as the main area of concern, proposing that the IASB defer the effective date of IFRS 9 for insurers and align it to the effective date of the future insurance contracts standard. The Council noted and discussed (i) the benefits of deferral as identified by EFRAG (ii) concerns identified by the FRC executive in respect of the proposal to defer and (iii) a proposed alternative approach put forward by EIOPA. Through discussion the following observations and suggestions were made:

- It was suggested that the response should encourage further consideration of the EIOPA solution in respect of the accounting for insurance liabilities and encourage the IASB to further explore a temporary removal of the existing restrictions on shadow accounting rather than the deferral of the effective date of IFRS 9 for insurers.
- It was suggested that the response should highlight the limitation of evidence as to the scale and extent of the problem for insurance companies and that the FRC should approach investors directly to ascertain whether they are capable of dealing with the additional complexities that would arise if no deferral is permitted.
- It was noted that the publication date of the future insurance contracts standard is unknown and that it is impracticable to defer the effective date to align with the implementation date of the future insurance contracts standard.
- The Council agreed that it would be appropriate to set out all of the concerns that have been identified with the proposal to defer excluding the issue of level of investment interest in the insurance industry.

5.7 The Council agreed with EFRAG's assessment that IFRS 9 is likely to result in significant implementation costs for preparers on transition to IFRS 9 but it did not agree that there will be significant on-going costs. The Council advised that the response be updated to reflect this view but suggested constituents should be asked a question on the matter at the constituent event.

5.8 SJON undertook to revise the response to reflect the advice of the Council and to reflect any views expressed at the constituent event on 22 June. The Council noted that the revised draft would be circulated to the Council for comment by email prior to submission.

The Council requested that the slides to be presented at the constituent event should be circulated to the Council for information.

6. Effective date of IFRS 15 Exposure Draft

6.1 The Council noted that the IASB has issued an Exposure Draft proposing the deferral for one year of the effective date for IFRS 15 Revenue from Contracts with Customers to 1 January 2018, with early adoption permitted.

6.2 The Council discussed draft comments letters to the IASB and EFRAG. The following suggestions were made:

- The Council suggested that the third paragraph in the draft response letter to the IASB should be amended to emphasise the importance of ensuring that a stable platform is established.
- It was suggested that the FRC should, at a future date, encourage the IASB to have regard to due process when considering any amendments to the IFRS 15. It is important that preparers are fully engaged in the development of the final standard and any fatal flaw review.
- In noting that the FASB may decide to defer implementation of Topic 606 for a period of 2 years the Council suggested that the fourth paragraph of the response letter to the IASB be removed.

6.3 Subject to the amendments set out at 6.2 the Council approved the draft comment letters to be issued.

7. Any other business

7.1 The Council noted that Section 410 of the Companies Act had been removed and that the reporting requirements that would arise as a result of the removal are inconsistent with the principle of clear and concise reporting. MM reported that the FRC was aware of the change and had advised BIS against the change.

7.2 There was no other business.