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Ernst & Young LLP
1 More London Place
London
SE1 2AF

Tel: + 44 20 7951 2000
Fax: + 44 20 7951 1345
ey.com

Susanne Pust Shah
Financial Reporting Council
8th Floor
125 London Wall
London
EC2Y 5AS

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Dear Ms Shah,

Invitation to comment – FRED 56 *Draft FRS 104 – Interim Financial Reporting*

Ernst & Young LLP welcomes the opportunity to comment on FRED 56 *Draft FRS 104 – Interim Financial Reporting* ('the Exposure Draft') issued by the Financial Reporting Council ('the FRC').

We support the FRC's objective in reforming financial reporting standards in the UK in a manner that will enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs. We also support the FRC's aim to have consistency with international accounting standards through the application of an IFRS-based solution unless an alternative clearly better meets that objective.

In this context, we agree with the proposed withdrawal of the ASB Statement – *Half-yearly Financial Reports* and its replacement with FRS 104 – *Interim Financial Reporting*.

However, we have the following concerns about the proposals in the Exposure Draft which we believe should be addressed before its issue as a Financial Reporting Standard:

- We have reservations about the proposal to withdraw the ASB Statement *Preliminary Announcements* as this would leave entities with no guidance concerning the preparation of what is still for many investors the first public announcement of price-sensitive information about the company's financial performance and year-end financial position. We suggest instead that the FRC considers updating the guidance.
- The application of the year-to-date approach to measurement is probably the most difficult aspect of interim financial reporting for both preparers and users. In our opinion, the illustrative examples in Appendices B and C to IAS 34 should be retained in FRS 104.
- We agree that FRS 104 should provide guidance for those entities whose annual financial reports are prepared using FRS 101. However, in our view, the proposed instruction in paragraph 3A to substitute references to FRS 102 with 'the equivalent requirements in EU-adopted IFRS as amended by paragraph AG1 of FRS 101' is not sufficient.

Should you wish to discuss the contents of our response, please do not hesitate to contact me.

Kind regards
Yours sincerely

Tony Clifford

Tony Clifford
Partner, Financial Reporting Group

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Appendix – Response to questions

Question 1—Withdrawal of the ASB Statement – *Preliminary Announcements*

Do you agree with the proposal to withdraw the Statement *Preliminary Announcements* issued by the Accounting Standards Board (ASB) in 1998?

If not, why not?

We acknowledge the FRC's reasons for proposing the withdrawal of the ASB Statement *Preliminary Announcements*, including the assertion that market practice has developed whereby today's preliminary announcements often exceed the minimum content prescribed by the Listing Rules.

However, many entities continue to issue a preliminary announcement in advance of their submission of the public announcement of the annual financial report required by DTR 4.1 and DTR 6.3.5, because the latter requires the full text of the annual report to be made available. Therefore, despite the requirement for a preliminary announcement having been withdrawn in 2007, it remains a key part in the annual financial reporting cycle of many entities and continues to represent the first public communication of a listed entity's full-year results and year-end financial position. The (now voluntary) preliminary announcement is still 'relied upon to provide timely, sufficient and accurate information to ensure an orderly and efficient market'. [ASB Statement Preliminary Announcements, Foreword]. It is also notable that the Introduction to the ASB Statement observes that such announcements 'often contain more information than the minimum required by the Exchange' but nevertheless the ASB chose to issue the Statement in 1998.

We are therefore concerned that the FRC proposes to withdraw the ASB Statement when, rather than being obsolete, the need for guidance on the content of a preliminary announcement is as necessary as it ever was. We suggest instead that the FRC considers updating the guidance, concentrating on what might be regarded as 'any significant additional information necessary for the purpose of assessing the results being announced' [LR 9.7A.1(5)] and providing guidance for preparers to reflect the references to half-yearly reports in LR 9.7A.1(3).

Question 2—Issue of FRS 104 and withdrawal of ASB Statement - *Half-Yearly Financial Reports*

Do you agree with the proposal to withdraw the Statement *Half-yearly Financial Reports* issued by the ASB in 2007 and replace it with interim financial reporting requirements based on IAS 34 *Interim Financial Reporting* as proposed in draft FRS 104 *Interim Financial Reporting*?

If not, please give your reasons and propose an alternative approach.

We agree with the proposed withdrawal of the ASB Statement – *Half-yearly Financial Reports* and its replacement with FRS 104 – *Interim Financial Reporting*.

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Question 3—Amendments to IAS 34 to adapt it for use by entities applying FRS 102

Draft FRS 104 proposes amendments to the reporting requirements in IAS 34 in order to adapt them for use by entities that apply FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* to prepare the annual financial statements. The Accounting Council's Advice to the FRC to issue FRED 56 highlights the key changes.

Do you agree with the proposed amendments? If not, please give your reasons.

We agree that the amendments to IAS 34 proposed in the exposure draft are appropriate, as they properly reflect the principle that interim financial reports should be prepared using the same accounting policies as are applied in an entity's annual financial statements.

In particular, the proposed requirements in paragraphs 8 to 8D and 15B(j) are consistent with the equivalent requirements in FRS 102; and the omission of certain paragraphs of IAS 34, such as paragraphs 5 to 7, 12 and 14 appropriately remove text expected to be irrelevant to an entity not applying IFRS. In addition, we believe that the addition of paragraph 16B provides useful guidance to entities issuing an interim report in their first year of applying FRS 102.

However, we have reservations about the FRC's proposal to omit from FRS 104 all of the illustrative examples that accompany IAS 34. The application of the year-to-date approach to measurement is probably the most difficult aspect of interim financial reporting for both preparers and users of interim financial statements. In our opinion, the illustrative examples in Appendices B and C to IAS 34 provide assistance in establishing the distinction between the treatment of periodic revenues and costs and those items that should be recognised at a point in time. Whilst it could be argued that, in any event, entities will probably refer to these examples via the hierarchy in Section 10 of FRS 102, we believe the FRC should consider their inclusion in FRS 104 itself, as this will help reduce diversity in practice.

Question 4—Application of FRS 102 by entities applying FRS 101

There may be a small number of entities that are required to prepare interim financial reports and apply FRS 101 *Reduced Disclosure Framework* to prepare the annual financial statements. Paragraph 3A of draft FRS 104 requires that these entities should read references to FRS 102 in draft FRS 104 as the equivalent requirements in EU-adopted IFRS as amended by paragraph AG1 of FRS 101.

Do you agree with this proposal? If you believe further changes are necessary to enable these entities to apply draft FRS 104 please state your recommendations and reasons for your proposal.

We agree that FRS 104 should provide guidance for those entities whose annual financial reports are prepared using FRS 101.

However, in our view, the proposed instruction in paragraph 3A to substitute references to FRS 102 with 'the equivalent requirements in EU-adopted IFRS as amended by paragraph AG1 of FRS 101' is not sufficient, on the following grounds:

1. Entities applying FRS 101 in their annual financial statements would usually refer to the relevant Standard or Interpretation under EU-adopted IFRS, and then apply the amendments in paragraph AG1. A similar approach to interim reporting would imply that the primary point of reference should be IAS 34 and not FRS 104. This distinction is relevant, since FRS 104 excludes the following disclosure requirements set out in IAS 34:
   - transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments [IAS 34.15B(k)];
   - changes in the classification of financial assets as a result of a change in the purpose or use of those assets [IAS 34.15B(l)]; and
   - for entities becoming, or ceasing to be, investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, the disclosures in IFRS 12 *Disclosure of Interests in Other Entities*, paragraph 9B [IAS 34.16A(k)].

   In addition, IAS 34.15B(h) requires an entity to disclose significant changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, when those assets or liabilities are recognised at amortised cost (as well as at fair value); and IAS 34.15B(j) provides no exemption from the disclosure of related party transactions involving a wholly-owned subsidiary in the same group.

   It would be helpful if FRS 104 clarified whether an entity applying FRS 101 in its annual financial statements should include these additional disclosure requirements.

2. A principle of both FRS 104 and IAS 34 is that interim financial reports should be prepared using the same accounting policies as are applied in an entity's annual financial statements. Accordingly, it would be appropriate for FRS 104 to include guidance on the extent to which entities that have chosen to take advantage of disclosure exemptions permitted under paragraphs 7 and 8 of FRS 101 are relieved from equivalent requirements in relation to their interim financial reports. For example, FRS 101.8(d) relieves a qualifying entity that is not a financial institution from the requirements of IFRS 7. However, by substituting the reference in FRS 104.16A(j) to paragraphs 11.43 and 11.48(e) of FRS 102 with 'the equivalent requirements in EU-adopted IFRS as amended by paragraph AG1 of FRS 101', such an entity would have to consider the need to provide these disclosures in its interim financial report. A similar issue would arise for an entity that acquired a set of assets and liabilities meeting the definition of a business under IFRS 3 and would be required under FRS 104.16A(i) to provide the disclosures set out in paragraphs B64, B66 and B67 of IFRS 3, despite the exemptions available in FRS 101.8(b) in respect of those paragraphs in relation to its annual financial statements.

We suggest that the FRC considers including in FRS 104 a section that clarifies what disclosures are required for an entity applying FRS 101.

Question 5—Informational value of FRS 104

Do you agree that applying draft FRS 104 will result in useful information for users of interim financial reports?

If not, what additional disclosures should in your view be included or which disclosures should be removed? Please give your reasons.

We believe that draft FRS 104 will encourage those entities not required to apply IFRS in their interim financial reports to provide information that is comparable with other issuers of interim financial information, whether reporting under IAS 34, FRS 101 or FRS 102. As such, we agree that applying draft FRS 104 will result in useful information for users of interim financial reports.