Financial Reporting Council

Minutes of a meeting of the Accounting Council held on Thursday 16 October 2014 in the Boardroom at 8th Floor, 125 London Wall, London, EC2Y 5AS

Present:	
Roger Marshall	Chair
Richard Barker	Council Member
Chris Buckley	Council Member (from minute 3)
Michael Gallagher	Council Member
Gunnar Miller	Council Member (to minute 9)
Liz Murrall	Council Member
Veronica Poole	Council Member (from minute 3)
Jeremy Townsend	Council Member
Mark Smith	Council Member
Pauline Wallace	Council Member
Observers:	
Lee Piller	FCA Observer (from minute 3)
Alison Ring	HMRC Observer (in place of Matt Blake)
Jim Sutcliffe	Chair, FRC Codes & Standards Committee
In attendance:	
David Andrews	Head of Organisational Development (Minute 5 only)
Anthony Appleton	Director of Accounting and Reporting Policy
Jenny Carter	Director of UK Accounting Standards, Accounting & Reporting Policy Team
Francesca Chittenden	Council Secretary
Annette Davis	Project Director, Accounting & Reporting Policy Team
Jennifer Guest	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
Tulsee Rughoobur	Finance & Performance Officer (minute 5 only)

Welcome and Apologies for absence

The Chair welcomed Jim Sutcliffe and Lee Piller to the meeting.
Apologies were noted from Mike Ashley (EFRAG observer) and Michael Kavanagh (IAASA Observer).

1. IFRS 15 - Revenue Recognition

1.1 The Council received an educational briefing on IFRS 15 – Revenue from contracts with customers. The purpose of the briefing was to provide Members with an overview of the new requirements in anticipation of future consideration of the EFRAG Endorsement Advice.

1.2 The Council noted that:

- IFRS15 will provide a single model for revenue recognition from contracts, replacing IASs 18 and 11 and multiple US GAAP pronouncements.
- At a high level IFRS 15 codifies best practice
- IFRS 15 sets out a five step process:
  1) identifying the contract
  2) identifying performance conditions
  3) determining transaction price
  4) allocating transaction price
  5) recognising revenue.
- Different sectors will be impacted to varying degrees by each step.
- There is an on-going debate as to the extent that insurance contracts contains financial instrument contracts and/or service contracts,
- The IASB is aware of potential issues in relation to the consistency of IFRS 15 with IFRS 4.
- It is expected that IFRS 15 will be applicable for years commencing on or after 1 January 2017 but that there is some pressure in the United States to delay implementation to 2018.
- Users are broadly content with the IFRS 15.
- EFRAG's draft endorsement advice on IFRS 15 is underway and will be presented to the Council in November.
- Reference to the concept of 'prudence' has not been retained in IFRS 15.

2. Minutes of the previous meeting and rolling actions

2.1 The Council approved the minutes of the Accounting Council meeting held on 11 September 2014 as an accurate record of the meeting. Subject to a revision to minute 6.4 and the inclusion of the word 'insurance' at minute 2.2.

2.2 The Council noted the rolling action log and that all actions were complete.

3. Director of Accounting Report

3.1 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:

EFRAG

3.2 The Council noted that:

- EFRAG had approved its Endorsement Advice (EA) and Effects study report on *Agriculture: Bearer plants* (amendments to IAS 16 and IAS 41).
- EFRAG had published the final report of the FRC, EFRAG and other National Standard Setters additional public consultation on leases. The Chairman reported that IASB were due to discuss a lengthy paper on the lease definition at its meeting the following week and that one of the two options under consideration is consistent with the views expressed by the FRC.

- Whilst the European Commission had not yet requested an EA from EFRAG in relation to IAS 9 *Financial instruments*, EFRAG TEG had begun considering the standard. It was also noted that the TEG are due to consider the standard in November but a draft EA would not be considered until the Commission has had a further discussion with Member States and sent its formal request for EA to EFRAG.
- EFRAG had revised its comment letter on the IASB's ED2014/02 *Investment Entities: Applying the Consolidation Exception (*Proposed amendments to IFRS 10) and that the revised comment letter was consistent with the views expressed by the FRC.

3.3 The Council noted that the ARC had met on 23 September and it had been confirmed that IFRS 14 *Regulatory Deferral Accounts* would not be considered for endorsement in the EU given that it is an interim standard with very little applicability in the EU.

3.4 The Council noted that the Accounting Standards Advisory Forum (ASAF) had met on 25 and 26 September and noted a summary of the matters discussed. AA reported that the issues identified by the FRC in relation to the IFRS 3 post-implementation review were very similar to issues raised by others, including the difficulty of applying fair value measurement, problems with the definition of a business, the level of separation of intangible assets and whether or not to amortise goodwill.

4. Director of Research Report

4.1 Andrew Lennard (AL) introduced a paper that provided an overview on current accounting research activities. The Council noted:

- That the work on 'cash flows' is progressing, a revised version of the paper that had been prepared primarily for IFASS, and was discussed by the Council in September, is to be presented to the IASB at its meeting on 22-24 October and that extracts of that paper will also be presented to the IASB's Capital Markets Advisory Committee and Global Preparers Forum meetings.
- A brief report on recent meetings of the World Standard Setters (WSS); the International Forum of Accounting Standard Setters (IFASS) and the first meeting of the IASB Research Forum.
- That the presentation given by Sue Harding on the FRC's Financial Reporting Lab at the WSS meeting had been well received.
- That plans for developing and issuing Bulletins in partnership with other standard setters under the 'Getting a Better Framework' initiative had been deferred until the 'fatal flaw' Exposure Draft of the IASB's Conceptual Framework had been issued.
- That interesting discussions had been held at the IASB's inaugural Research Forum in Oxford and at the Accounting Council's Academic Panel the previous day.

5. FRC risks and impact on work of the Accounting Council

5.1 AA introduced a paper that provided an introduction to the FRC Risk Register and highlighted which risks are of the most relevance to the work of the Accounting Council.

5.2 David Andrews (DA) provided an overview of the FRC's general approach to risk management and the Council noted that a thorough approach to developing and maintaining the Risk Register is undertaken and a wide range of views are sought to inform that development.

5.3 Jim Sutcliffe (JS), Chair of the Codes & Standards Committee (CSC), highlighted a range of risks areas that the CSC would like the Council to consider more fully when developing its advice. The Council noted that in order to improve the working relationship between the CSC and the Council and avoid the risk of the FRC appearing disconnected, the Council is encouraged to more explicitly consider the FRC mission in developing its advice.

5.4 The Council welcomed the Risk Register and the views expressed by JS. The Council moved on to discuss the strategies for addressing the risks that had been identified, how the Council could assist, and whether any risks have not been captured. Through discussion the following points and observations were made:

- Regulators can be viewed negatively as self-perpetuating, the FRC needs to mitigate this risk by demonstrating its relevance through the development of standards and guidance that reflect the needs of users and are current, reflecting the world we are in and the ever increasing reliance on technology.
- The FRC should be proactive and understand the extent of any demand to look at preliminary announcements. The Council highlighted that preliminary announcements play an increasingly important role in investment decisions and the FRC should acknowledge this.
- The FRC should consider how, with regards to the UK economy, accounting and reporting reflect and are consistent with long-term value creation.

5.5 The Council noted that the FRC is approaching the final year of its 2013-16 strategic plan and that work to develop the 2016-19 strategy was well underway. MM confirmed that the points raised through discussion would be considered when the risk register is updated to reflect the 2016-19 strategic plan and that input would be sought from the Council to inform the revised risk strategy.

6. Insurance Contracts

6.1 Seema Jamil-O'Neill (SJON) introduced a paper that summarised the current IASB accounting model for insurance contracts. The Council noted that the current model addresses the majority of concerns that had been made by respondents to the 2013 ED but issues in relation to participating contracts remain. SJON reported that the IASB intend to conclude deliberation on the current model by the end of 2014 so that the final standard can be published in 2015.

6.2 SJON explained the current model and highlighted the concerns that have been raised by the insurance industry in relation to that model. It was noted that there are concerns in relation to:

- The scope, which has become so narrow that no truly participating contract will be within the scope of this exception to the main measurement model;

- The extent to which economically similar contracts may be accounted for differently due to the differences in the way the contracts are drawn.
- The criterion requiring there to be a fixed or determinable minimum amount the entity must retain, given that in most participating contracts (but especially with-profits contracts) the participation rate between the insurer and the policyholder is set out in the contract as a maximum amount that may be retained by the insurer which means that no minimum amount retained by the insurer is fixed at the outset of the contracts.

6.3 The Council discussed the recommendation that the FRC partner with other National Standard Setters (NASS) to write to the IASB to set out concerns with the approach being taken for accounting for participating insurance contracts and to highlight the need for public fatal flaw review. Through discussion the following observations and suggestions were made:

- Steps need to be taken to ensure the IASB fully understand industry practice and that the insurer only retains a percentage of the *return* on the participating assets, not a percentage of the asset itself
- The industry needs to be encouraged to identify a solution, or to present a consistent view, as to what the industry wants the standard to achieve. An issue that may be preventing the IASB reaching a solution could be that many differing views are being presented and to address this one consistent UK view needs to be developed.
- One solution may be to exclude participating contracts entirely.
- The FRC should identify which NASS have an insurance model that is broadly similar to the UK model, noting that the Canadian and European models are very different.
- The Council noted there are concerns in relation to the transition proposals and that there is a disconnection between the timing of this standard and IFRS 9.

6.4 It was concluded that the FRC should delay writing to the IASB until the FRC is in a position to recommend a solution, which is supported by the UK industry.

7. Review of IAS Regulation Questionnaire

7.1 Annette Davis (AD) introduced the draft FRC response to the public consultation the European Commission is undertaking as part of its evaluation of the IAS Regulation. The Council noted that the Commission is aiming to assess the actual effects of using IFRS and that the results of the consultation will feed into a larger evaluation report which the Commission will present to the European Parliament and the Council of the EU by 31 December 2014.

7.2 The Council noted that the questionnaire had been completed in liaison with colleagues in the FRC Conduct Division and that the questionnaire would be also discussed by the FRC Codes & Standards Committee before submission.

7.3 AD invited the Council to comment on the completed questionnaire, through discussion the following observations and suggested amendments were made:

- It was suggested that some of the responses could be interpreted to be more negative than is intended and that the Executive should look to address this. The

response should make it clear that we do not consider that the Regulation needs amending.
- The Council highlighted the importance of ensuring the responses to the questionnaire are consistent with the FRC statement that was issued in response to the Maystadt recommendations, in particular the view taken by the FRC in response to the Maystadt recommendations on financial stability.
- The Council discussed the Q22 and Q22.1 in detail and concluded that the endorsement criteria are appropriate, however, the Council suggested that the Executive revise the comment to set out that whilst the criteria is appropriate, better clarification of whether something is “conducive to the European public good” is required. The clarification should explain that a range of factors needs to be considered and that each of the factors may be given different weighting depending on the standard or amendment that is being considered for adoption. The Council advised that the response to Q22.1 should not encourage more explicit reference to prudence.
- The Council suggested that the Executive reconsider the ordering of the comment given in response to Q26 to place greater emphasis to avoidable complexity.
- The Council suggested that the response to Q29 should be revised to reflect the True and Fair override.
- The Council advised the Executive to amend the answer to QPA.1 to state that the administrative and regulatory burden arising from the ongoing application of IFRS is not significant on the basis that the UK has always been subject to heavy regulation.

8. Pension Research Accounts Group SORP

8.1 Jennifer Guest (JG) introduced the final draft Pensions Research Accounts Group (PRAG) SORP, the FRC statement on the PRAG SORP and an analysis of responses to the consultation. The Council noted that the SORP had been considered and approved by both the UK GAAP Technical Advisory Group and the PRAG Executive and that it is the intention of the PRAG Executive to issue the SORP at its AGM on 25 November.

8.2 JG summarised the actions that had been taken by the PRAG SORP working party in response to the advice given by the Council at its September meeting. The Council was content with the actions that had been taken and the corresponding changes that had been made to the SORP. The Council noted that the SORP working party had considered the possibility that the SORP recommend further additional disclosures in relation to transaction costs, but, on the basis that the Government would shortly be introducing standardised transaction cost reporting for pension schemes, had concluded it would not be appropriate for the SORP to include further, potentially inconsistent recommendations. The Council noted that given the wide ranging and diverse pension landscape, they considered this to be appropriate.

8.3 The Council queried whether the provision set out in the SORP to defer recognition of revenue from auto enrolment to the fourth month is a correct interpretation of FRS 102 and requested that the matter be discussed with the PRAG SORP working group before finalisation. Subject to a review of the provision with regard to auto enrolment the Council agreed its advice to the Codes & Standards Committee to recommend that the FRC Board approve the issue of the SORP and issue the FRC statement on the SORP.

9. Foreword to Accounting Standards – Revision

9.1 The Council noted that the FRC has in issue a *Foreword to Accounting Standards* (the 'Foreword)' which explains the scope and application of accounting standards issued by the FRC. It refers to 'accounting standards' for the purposes of company law and specifically states that accounting standards developed by the FRC are designated Financial Reporting Standards (FRSs). JC invited the Council to consider the recommendation that the FRC amend this particular within the Foreword to enable FRSs to cover other aspects of financial reporting, such as interim reporting. JC highlighted that the recommended provision would ensure the FRC is in a position to reflect the FRCs new standards and guidance framework. The Council noted that the recommendation had been considered and approved by colleagues in the FRC Conduct Division.

9.2 Through discussion the following observations were made:

- It was clarified that it would be made clear in each pronouncement whether that particular pronouncement is an accounting standard or whether it is intended to address other aspects of financial reporting.
- It was clarified that the FRC will be unable to require the mandatory application of any pronouncements (other than accounting standards) and that responsibility for imposing and monitoring application of such pronouncements will rest with others. AA confirmed that the FRC would only issue such pronouncements if the appropriate structure to support the application is in place, guidance around enforceability will be made clear in the preface of each pronouncement.

9.3 The Council noted that further amendments to the Foreword would be necessary when the EU Accounting Directive is implemented and suggested that as part of that the Executive take that opportunity to fundamentally review the Foreword. The review should include a revision of the order of the introductory paragraphs, the inclusion of a statement to provide clarity as to what constitutes Companies Act accounts and to reflect the revised True & Fair statement.

9.4 The Council agreed its advice to the Codes & Standards Committee to issue the revised Foreword to Accounting Standards.

10. FRED 57 – Draft amendments to FRS 101 (2014/15 Cycle)

10.1 JC introduced a paper which set out an analysis of, and recommended actions arising from, the second annual review of FRS 101 Reduced Disclosure Framework. The Council noted that the review had been undertaken to ensure that FRS 101 continues to maintain consistency with EU-adopted IFRS and continues to promote efficiencies in reporting for groups.

10.2 The Council noted the analysis and that both the analysis and recommendations had been considered and approved by the UK GAAP Technical Advisory Group (TAG). Through discussion of the recommendations it was agreed that:

- FRS 101 should be amended to provide an exemption against:
    I. paragraph 18A of IAS 24 *Related Party Disclosures* on the basis that FRS 101 already allows an exemption against paragraph 17 (to avoid gold

plating the Directors' remuneration disclosure requirements) and in recognition of the fact that the requirement to disclose Directors remuneration is covered under company law; and

    II. the requirement of paragraphs 6 and 21 of IFRS 1 First-*time Adoption of International Reporting Standards* to prepare and present an opening statement of the financial position on first-time adoption of IFRS.

- Amend the application guidance to FRS 101 to reflect:
    I. amendments made to the underlying text of paragraph 40 of IFRS 3 *Business Combinations*; and
    II. an editorial amendment to delete paragraph 33(b)(iv) of IFRS 5 *Discontinued Operations and Assets Held for Sale.*

- No amendments are required in relation to *IFRS 15 Revenue from Contracts with Customers* as it is too early to determine whether any exemptions should be permitted given that the standard has yet been applied by entities.
- *Consideration of Equity Method in Separate Financial Statement* (Amendments to IAS 27) is deferred until the 2015/16 cycle, following implementation of the Accounting Directive.
- No amendments are required to IFRS 9 *Financial Instruments*; however, FRED 57 will make reference to the revised requirements of IFRS 7.
- No amendments are required to any other IASB amendment of IFRSs issued in the last 12 months.

10.3 The Council noted that the amendments would be incorporated in to FRED 57, which would be presented to UK GAAP TAG for review on 6 November, the Council for approval of its advice on 13 November, the Codes & Standards Committee on 24 November and the FRC Board for approval for issuance on 10 December.

11. Residents' management companies

11.1 The Council noted that the FRC has consulted on residents' management companies (RMCs) twice in response to a call from the ICAEW to clarify whether RMCs act as agents or principals and to highlight the fact there is diversity in practice. The Council noted that on seeing the proposed drafting for insert a new subsection into Section 34 *Specialised Activities* of FRS 102, the UK GAAP TAG had been strongly opposed on the grounds of cost benefit and had suggested the Executive consider a more proportionate approach.

11.2 JC reported that the Executive had reflected on the views presented by UK GAAP TAG and respondents to the earlier consultations and had preliminarily concluded that the most appropriate course of action would be to issue a pronouncement in the Accounting Council's advice to clarify that the RMCs act as principals. Feedback to the present consultation on small company accounting standards will also be taken into account, however for the time being the Council noted that the approach would not prevent complete diversity in practice, but the Council considered that the level of diversity would be acceptable and that the issue of a pronouncement would be proportionate, would show that the FRC is 'doing something' to bring the issue to a close and would not set a precedent for future requests for sector specific amendments.

11.3 The Council noted that whilst the proposed pronouncement would not set out how, practically, the statement should be applied; publication of the FRCs view through the pronouncement should encourage those who currently produce dormant accounts to recognise that they should not. The Council suggested that the Institute should be encouraged to communicate this view amongst its members.

12. Any other business

12.1 There was no other business.