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FINANCIAL REPORTING FACULTY

JULY 2014
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STRAIGHT TALKER
IN CONVERSATION WITH THE THE 100 GROUP'S RUSS HOULDEN

THE END IS IN SIGHT
BRINGING YOU UP TO DATE WITH THE NEW UK GAAP

CATALYST FOR SUCCESS?
COULD <IR> CHANGE CORPORATE REPORTING?

ALL ABOARD
The new IFRSs arrive – all at once

A FACULTY TECHNICAL PUBLICATION

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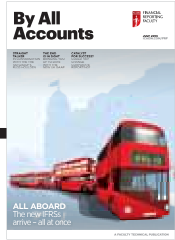

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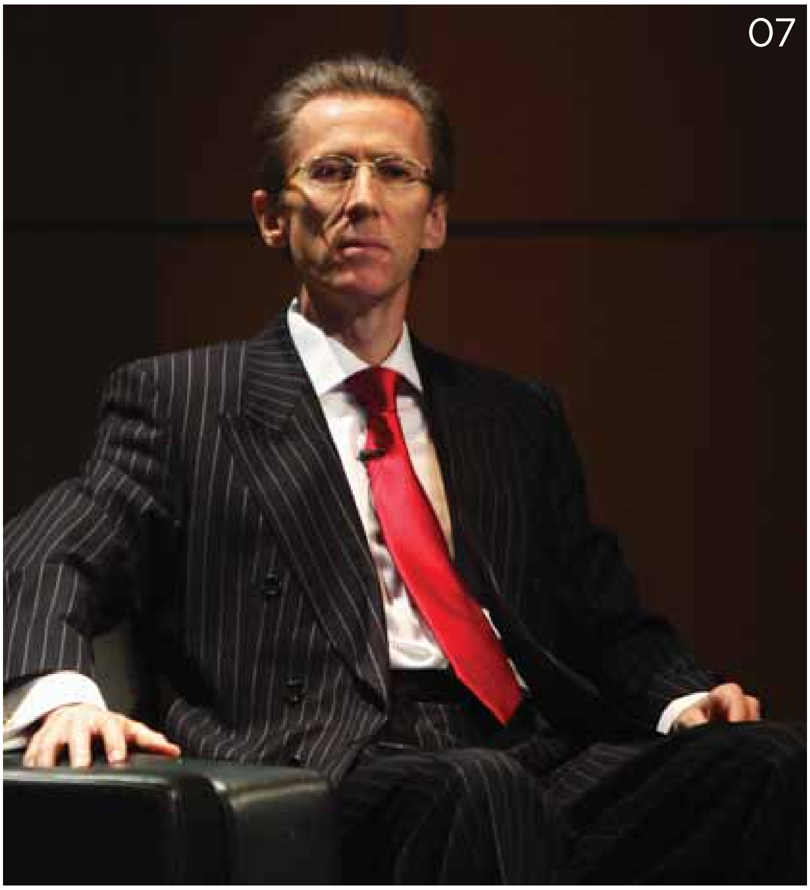

COVER: DAN MURRELL

"Accounts are meant to make us accountable: yet at a time when everyone is migrating to global standards, we are left with a very inconsistent framework"

Bob Humphreys, Oxfam's finance director, on an international accounting standard for the not-for profit sector

The only constant

FINANCIAL REPORTING FACULTY

IFRSs are a bit like buses – you patiently wait around for ages for one to arrive and then suddenly several come along all at once.

The last big flurry of new standards was back in May 2011 when the IASB issued IFRSs 10, 11, 12 and 13 after completing its financial crisis-related projects on off-balance sheet activities, joint arrangements and fair value measurement. Since then there has been lots of sound and fury but in terms of actual standards, just a few revisions here and some narrow-scope amendments there.

Until now that is, as it's suddenly all hands to the pump once more as a cluster of new arrivals are upon us. What began as a trickle when the IASB issued an interim standard on rate regulated activities is fast developing into a flood, with the long-awaited new standard on revenue recognition now published and the remaining pieces of the revamped financial instruments standard expected soon. Although these new global standards will not be mandatory for some time yet, there is nonetheless much to think about and planning ahead is essential.

But sometimes it's good to get away from the detail of individual standards and think about the bigger picture. We should perhaps remind ourselves that above all else financial statements are there to serve the needs of investors, and that this can only be achieved well if they convey a consistent and coherent story that is told in a universally recognised language. It is issues such as these that are on the mind of United Utilities CFO Russ Houlden as he settles into his new role as chair of The 100 Group's financial reporting committee. I'm sure you'll find our interview with him - which looks at these and other issues keeping the finance directors of the UK's biggest companies awake at night - an interesting read.

Finance directors at smaller UK private companies are, however, probably more worried about the implementation of the UK's new financial reporting regime right now. Since the launch of the revamped UK GAAP in early 2013, we have seen the publication of a number of proposals that will see the new standards amended even before they become effective in 2015. Most significantly, changes have been proposed that would revise the fledging standard's requirements in relation to debt instruments such as bank loans and almost completely rewrite the rules on hedge accounting. As the adoption date looms ever larger, the goalposts are - in many ways - still moving.

At the same time, a new UK regime for micro-entities has been launched. This has contributed to the ongoing debate about the future of the FRSSE and it seems that proposals are afoot that may ultimately see that standard withdrawn.

This edition contains much to ponder on. In the world of financial reporting, change it seems is the only constant. But, as ever, your faculty is here to help.

Nigel Sleigh-Johnson

Dr Nigel Sleigh-Johnson FCA
Head of Faculty

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Faculty news

PRAISE FOR OUR REPORT ON DISCLOSURES

Since its publication late last year, the faculty's thought leadership paper *Financial Reporting Disclosures: Market and Regulatory Failures* has proved to be an influential contribution to the global debate about the length and complexity of financial reports. Praise has been forthcoming from various quarters and we have been invited to contribute to the work of the US FASB and the Japanese Ministry of Economics, Trade and Industry as they begin their own projects on disclosures.

The report looks at the paradox that while many complain of information overload in financial reporting disclosures, others complain that they are still not getting all the information they need. It can be downloaded from icaew.com/bettermarkets

LATEST FACTSHEETS

Our factsheets – designed to help faculty members identify how rules and regulations impact on their financial reporting – continue to prove popular, and new titles are being added all the time.

We have recently published our annual *2014 IFRS accounts* and *2014 UK GAAP accounts* factsheets, both of which are packed with practical advice and tips. We've also recently published a factsheet on *Micro-Entities' Accounts* which looks at the new regime for the UK's smallest companies, setting out the qualifying criteria and exemptions available. Many of our existing titles have also been updated to reflect the latest developments.

You can download our full range factsheets at **icaew.com/frffactsheets**

'FACULTIES ONLINE' PRODUCT LAUNCHED

As a Financial Reporting Faculty member, you already benefit from the technical information and support that we provide. ICAEW is offering a new service, Faculties Online, where you can receive the benefits of online access to all seven faculties and the three communities for a single fee. Subscription includes a regular e-bulletin showcasing the latest collective resources of the faculties, and technical updates on key developments, legislation, trends and practical advice. You can join at icaew.com/facultiesonline for an introductory rate of £200 plus VAT.

The Faculties Online service does not provide access to the IASB's eIFRS service or to Financial Reporting Faculty webinars.

PAUL DRUCKMAN APPOINTED TO FACULTY ADVISORY GROUP

We are delighted to announce that Paul Druckman has joined the faculty's advisory group. Paul is chief executive officer of the International Integrated Reporting Council (IIRC) and a past president of ICAEW. He is also formerly a director of the UK Financial Reporting Council and a member of the City Takeover Panel. Paul's high-profile work on sustainability has included chairing The Prince's Accounting for Sustainability Project Executive Board and the FEE Sustainability Group.

Paul joins a group of highly influential figures from business, academia, the user community, regulators and the profession who meet once or twice a year to consider the wider financial reporting agenda and provide general advice to the faculty's board on trends and developments that might impact on the scope and direction of faculty activities. We're sure Paul will make a highly valuable contribution to this group.

The faculty now has its very own Twitter account – keep up-to-date with the latest financial reporting developments and news **@ICAEW_FRF**

FACULTY AGM

On 15 May, faculty chair Stephanie Henshaw presented our 2013 annual review and shared the year's highlights when the faculty AGM was held at Chartered Accountants' Hall. It formally brought the curtain down on a highly successful 12 months in which we not only significantly increased our individual membership but also welcomed a range of new corporate members.

The AGM also saw us saying a fond farewell to Donald Broad, who has retired from his role as Group Financial Controller of Smiths Group plc and has stepped down from the faculty board. Donald has been a member of the board since the faculty was launched in December 2008. We will miss his wit and wisdom and wish him well in his retirement.

GET UP TO SPEED WITH OUR NEW CPD COURSES

ICAEW is now offering a wide range of CPD training, including courses on IFRS, the new UK GAAP and US GAAP and specialist courses for the banking and insurance sectors. Courses are also available on an in-house basis, meaning that the training can be tailored to specifically meet your requirements and include examples and scenarios that are 'real life' issues to your business, making the training highly engaging, insightful and fun.

For more information contact **vivek.mehan@icaew.com**

CATCH UP ON OUR WEBINARS ON THE NEW UK GAAP

Over the last 18 months or so, the faculty has run a series of webinars looking at different aspects of the new UK GAAP. These webinars – which form a key part of efforts to raise awareness of the new financial reporting regime – have proved very popular, attracting a total of nearly 2,000 attendees. Topics covered include an overview of the new regime, an introduction to FRS 102, preparing to transition to FRS 102, the tax implications of FRS 102, accounting for financial instruments and the reduced disclosure framework. But don't despair if you missed any of them, as they are all available to watch again at **icaew.com/frfwebinars**

FACULTY EVENTS

SIGN UP NOW FOR OUR IFRS AND UK GAAP CONFERENCES

The faculty's fourth annual IFRS conference will take place on 9 December 2014. Our keynote speaker will be IASB vice-chair Ian Mackintosh. Ian will be joined by leading-edge speakers from business and the profession as we look at ongoing changes in the world of international financial reporting.

Meanwhile, our second annual UK GAAP conference will take place on 24 October 2014. As the implementation date of the UK's new financial reporting regime looms ever larger, the goalposts are – in many ways – still moving. As you grapple with transition, this conference will bring you up-to-date on all the latest developments and make sure that you are aware of all the new and emerging issues.

INFORMATION FOR BETTER MARKETS CONFERENCE

Our annual Information for Better Markets conference will be on the theme of 'capital: reporting, regulation and resource allocation'. It will be held at Chartered Accountants' Hall in London on 15-16 December 2014. Speakers will include the distinguished economist Professor Sir Partha Dasgupta on 'disregarded capitals: what traditional accounting ignores' as well as other leading academics and practitioners. Attendance at this major thought leadership event is free of charge.

FACULTY READY TO HIT THE ROAD ONCE MORE THIS AUTUMN

Following last year's record-breaking success, the faculty will once again take to the road this autumn. Our UK roadshow series will provide a detailed look at the new UK GAAP regime. We'll also be running a small number of updates on the latest IFRS developments. Events will be held throughout England and Wales.

To find out more about the events discussed on this page visit icaew.com/frfevents

A consistent and coherent story

The faculty's Nigel Sleigh-Johnson and Eddy James talk to **Russ Houlden**, CFO of United Utilities Group plc, chairman of the Audit Committee of Orange Polska SA and chairman of The 100 Group's Financial Reporting Committee

It is perhaps surprising how few ICAEW members have heard of The 100 Group. But the body that represents the views of the finance directors of the UK's FTSE 100 has been quietly lobbying government, regulators and standard-setters for almost 40 years, influencing taxation, corporate governance, capital market regulation, pensions and financial reporting policies.

With such a diverse range of interests, The 100 Group is organised through a structure of committees, including one that focuses on financial reporting issues. Since November 2013 this committee has been chaired by Russ Houlden, the CFO of United Utilities. We met him at United Utilities' Mayfair offices one early spring day to discuss the issues that are keeping the finance directors of the UK's biggest companies awake at night.

The 55-year old – who has also been CFO of Telecom New Zealand and the global law firm Lovells (now Hogan Lovells) and the finance director of various divisions of BT and ICI – recognises that financial reporting is very much in the firing line right now, with critics saying that the financial statements are overly complex and that key messages are increasingly lost among lengthy disclosures and regulatory jargon. But he also has some very firm ideas on what needs to be done to change the increasing perception that financial statements are of little relevance to investors.

“Financial statements should not become some sort of general purpose document that acts as a repository for information of interest to all and sundry”

BACK TO BASICS

Going back to basics wouldn't be a bad start, says Houlden. “Financial statements should be focused on the needs of debt and equity investors. That is their primary purpose. They should not become some sort of general purpose document that acts as a repository for information of interest to all and sundry. It is impossible to meet the needs of all stakeholders in a single document.”

Many would agree that the financial statements do appear to have become something of a dumping ground in recent years. Disclosures on topics such as employee diversity and human rights have been added. But Houlden feels that investors are interested in something more fundamental: “For the financial statements to provide investors with decision-useful information, they should clearly set out the company's strategy, and this should be supported by financial and non-financial performance measures. They must tell a consistent and coherent story. That may sound straightforward, but when you have different policymakers and standard-setters all providing their pull on one particular component, it is actually very challenging.”

GLOBAL STANDARDS

Indeed, there is an increasingly wide array of regulators telling companies what should appear in their financial statements. Foremost among them is the IASB, whose IFRSs - which are now used in well over 100 countries worldwide and are mandatory for FTSE 100 companies - have been heavily criticised in some quarters. However, Houlden is a keen supporter of the international standards. As he says: “Business is global, so a single, high-quality, global accounting language is essential. I am therefore a strong supporter of IFRS. Investors want comparability and that can only be achieved if we all adopt the same standards.”

Some might say that the goal of a truly global set of accounting standards is impossible, especially as efforts to converge IFRS and US GAAP are on hold. Others would like to go back to the ‘good old days’ of UK GAAP, while the creation of a European GAAP has been mooted in some quarters. But Houlden believes there is no going back, telling us: “Globalisation is here to stay, which means global standards are essential. While the creation of a truly global set of standards may take another 10 years or more, it is inevitable. Those who want to turn back the tide are like King Canute sitting on the beach.”

However, this doesn't mean Houlden offers his unconditional support to the IASB. As he explains: “Just because I believe in one accounting language, it doesn't mean that I agree with every individual standard.”

CONFLICTING MESSAGES

But those preparing the financial statements of FTSE 100 companies have much more to worry about than just IFRSs.

In the wake of the financial crisis, the spotlight remains very much on what can be done to improve what they report. The sheer number of initiatives and conflicting messages that are being given out is a cause of great frustration for Houlden: “One of the biggest issues we face across a number of our committees is the inconsistency of the guidance issued by various different bodies, much of which seems to be pulling in opposite directions. We've got the strategic report, the integrated report, ESMA's proposed guidelines on alternative performance measurement and the FRC's cutting clutter initiative, among others. Some of these proposals call for more disclosure, while others call for less. Some would like more focus on IFRS numbers, while others would like more focus on the strategic and economic story, which is often not well reflected in IFRS. Some blame standard-setters for disclosure overload, while others say companies could do more to eliminate immaterial disclosures. It can be very confusing.

“We can only produce one annual report, so it would be great if we could all agree on what it should contain. But you cannot tell me that the ESMA consultation is consistent with the strategic report or the integrated report. Nor can you tell me that the cutting clutter initiative is consistent with what the IASB are doing.”

Houlden is particularly concerned about ESMA's proposals. Investors increasingly look to such non-GAAP measures for insights

ABOUT THE 100 GROUP

The 100 Group represents the views of the finance directors of FTSE 100 and several large private UK companies. Its member companies represent almost 90% of the market capitalisation of the FTSE 100, collectively employing over 7% of the UK workforce and in 2012, paid or generated taxes equivalent to 14% of total UK government receipts.

The 100 Group can trace its origins back to 1975, when a group called The 100 Group of Chartered Accountants was formed. At that time, its members included a number of chief executives and company chairmen but more recently it has been limited to those with a current role in finance.

The overarching objective of The 100 Group is to promote the competitiveness of the UK for UK-based global and domestic companies, for the benefit of its members, the UK economy and long-term growth of the UK.

into a company's performance and while the proposals would not ban or limit their use, they do worry him: "Under the proposals, non-GAAP measures would have to be presented with less prominence than GAAP information. But doing so may make communication with investors worse rather than better. There are often good reasons why companies need to adjust their performance measures so that they accurately reflect their economic performance. If unadjusted GAAP numbers have to be given primacy it will make it harder for companies to tell their underlying economic story."

WORKING TOGETHER

Finding a way forward is a challenge, but Houlden thinks that a clear message needs to be sent to the myriad bodies looking to shape the financial statements of the future: "Investors and preparers often agree on what the best solution is. We must ensure that our voices are clearly heard. If we don't, it is too easy for the standard-setters to become detached from reality and to start satisfying their own egos. And that is when we end up filling the financial statements with clutter that investors don't really want and which is impractical or massively expensive for preparers to produce."

GETTY

Collaboration seems to be high on Houlden's agenda. In the past The 100 Group has sometimes been thought of as rather secretive and inward looking, but all that seems to have changed now. As Houlden puts it: "If we are to ensure that our views are given sufficient weight, we need to use as broad a range of influencing methods as possible – working not only with investors, but also with similar groupings of listed companies across Europe and with influential bodies such as the FRC and ICAEW here in the UK."

There's no doubt that Houlden is an interesting character. We look forward to working closely with him and his colleagues at The 100 Group.


Eddy James is a technical manager in the faculty and **Nigel Sleigh-Johnson** is head of the faculty

THE HEDGE MAZE: FINDING THE WAY

Jane Hurworth outlines some of the practical implications of the IASB's new general hedge accounting model

LUCIANO LOZANO / IKON

In November 2013 the IASB issued a new chapter of IFRS 9 *Financial Instruments* to replace the general hedge accounting guidance in IAS 39. The new model introduces some significant improvements by permitting entities to reflect better their risk management activities in the financial statements.

IFRS 9 is expected to be mandatory for accounting periods starting on or after 1 January 2018, although early application will be permitted (subject to EU endorsement where applicable).

However, to ease concerns in the financial sector, IFRS 9 includes an accounting policy choice whereby entities can elect to adopt IFRS 9 hedge accounting on the mandatory effective date, or continue with IAS 39 for all hedge accounting until the effective date of the future new standard on accounting for macro hedging.

NEW CONCEPTS

Although the new model has been developed from the building blocks of IAS 39, there are some new concepts that will have a significant impact in the future. In this article we will touch on some of the implications of the new guidance. However, in order to obtain a detailed understanding of the changes it will be necessary to read the standard.

Entities will need to review existing hedge relationships to confirm continued eligibility under IFRS 9. While it is expected that most existing relationships will remain eligible, the new standard introduces some important changes. Most significantly, effectiveness testing will no longer focus on the 80% to 125% bright line quantitative analysis. Only a prospective test will be required, which in many instances will be qualitative, requiring judgement. However, retrospective ineffectiveness will still need to be calculated and recorded.

The IFRS 9 effectiveness test has three criteria: existence of an economic relationship, fair value changes not dominated by credit risk and an appropriate hedge ratio. Considerable thought is required as to how the entity will determine that a hedge relationship meets the new effectiveness criteria, using qualitative principles, or quantitative analysis if required.

Hedge documentation remains core to the new model. Prior to transition, documentation should be reviewed and updated to reflect the new language and requirements. Careful attention should be given to the description of the hedge objective, as if this is deemed to have changed subsequently, the hedge relationship must end. In addition, IFRS 9 requires that hedge documentation is kept up to date, so that changes in the expected performance of the hedge relationship are reflected.

NEW POSSIBILITIES

A major advantage of IFRS 9 is that it will now be possible to designate risk components for exposures other than financial instruments, as long as the risk component is separately identifiable and reliably measurable. Where risk components are contractual ie, formulaic pricing specifying the market index being managed, it should be straightforward to demonstrate that the risk component meets this requirement. An example would be contracts for the supply of natural gas for which the price is contractually linked to a gas oil benchmark price.

Where risk components are not contractual, additional analysis is required both upfront and on an ongoing basis to demonstrate why and how the risk component meets the separately identifiable and reliably measurable requirement. Consideration of the market structure and pricing of the whole hedged item is required to demonstrate that the risk component has a distinguishable effect on changes in its cashflows or fair value. For example, how does the price of crude influence the price of jet fuel? This will require collation of pricing data over a period of time and involve areas of the business that have not traditionally been involved in hedge accounting, such as those in front line pricing and procurement.

Some of the changes introduced by IFRS 9 may cause entities to reconsider aspects of their economic hedging activities. For example, hedging with options may be viewed as more attractive than under IAS 39, as volatility from time value can be deferred in OCI, rather than recognised in P&L. However, changes to economic hedging strategies will take time to implement, involving changes to risk management oversight, systems, processes and ultimately reported results.

NEW PROCESSES

While the basic hedge accounting entries are unchanged in IFRS 9, a number of new concepts – such as the ability to partially de-designate and the requirement to rebalance hedge relationships in some circumstances – have been introduced that require changes to accounting processes and general ledger structure. Specifically, hedge accounting processes will need to accommodate changes in the volume of hedged item and/or hedging instrument without ending the hedge relationship.

In most circumstances, application of the new guidance is prospective, so all IFRS 9 hedge designations must be in place by the date of transition. This is particularly relevant for cash flow hedges if the entity wishes the IFRS 9 designations to be considered extensions of existing relationships. However, where an entity wishes to enhance effectiveness of existing hedge relationships, utilising improvements within IFRS 9, in some circumstances this will require de-designation of IAS 39 relationships and the start of new hedge relationships on transition.

NEW DISCLOSURES

There are also new disclosures which aim to better reflect the linkage between risk management activities and how hedge accounting is applied in the financial statements. There is an expectation that disclosed information will be specific to an entity's own risk management practices and be presented in a single place in the financial statements. Meeting these disclosures requirements will involve considerable planning, not least the communications strategy for the additional information provided. ■

Jane Hurworth is an executive director at EY

HELEN WALSH
HSBC

Hedge accounting is widespread within many financial institutions, although it is not applied to all economic hedges, as a consequence of the strict rules and formal documentation required.

IFRS 9 changes the focus of hedge accounting to try to create a link with risk management activity. The new model in IFRS 9 allows more flexibility of hedged items and hedging instruments, and permits more efficient use of options and forwards.

Financial reporting by banks is not expected to be significantly impacted by the new model, although it may present operational challenges. The three key considerations for banks are:

- the more formal link between risk management and hedge accounting will mean that revised documentation will be required;
- changes to practice in specific situations will have a related operational impact; and
- the more onerous hedge accounting and risk management disclosure requirements will mean these have to be redesigned and expanded.

Banks will be closely following the discussions around macro hedge accounting, which will have a much greater impact on the financial industry sector.

SIMON INGALL
Shell

Of all the changes that IFRS 9 brings, the hedge accounting reforms could have by far the most significant benefit for Shell. This is because IAS 39's requirements either prohibit hedge accounting for many of the risk mitigation transactions that Shell enters into, or make hedge accounting prohibitively onerous to apply. Thankfully, most of the new requirements specifically address these issues, so Shell broadly welcomes them.

Risk management systems will need to be adjusted to deal with the mechanics of the hedge accounting requirements

One of the simpler reforms is the change to IAS 39 allowing designation of physical contracts at fair value through profit or loss, which will match the movements in such contracts' fair values against the instruments taken out to hedge them without formally applying hedge accounting.

The ability to apply hedge accounting to risks with similar but not identical risk profiles and the easing of restrictions on hedge accounting for partially hedged risks and groups of risks will be of particular benefit.

Across the board, the speed with which the reforms are taken up by companies may vary however. Risk management systems will need to be adjusted to deal with the mechanics of the hedge accounting requirements and so it may take some time before the benefits of improved financial reporting are fully realised.

IFRS round-up

Eddy James provides a round-up of the latest IFRS developments

IASB ISSUES INTERIM STANDARD ON REGULATORY DEFERRAL ACCOUNTS

The IASB has issued IFRS 14 *Regulatory Deferral Accounts*. The aim of this interim standard is to enhance the comparability of financial reporting by entities that are engaged in rate-regulated activities.

Many countries have industry sectors that are subject to rate regulation, whereby governments regulate the supply and pricing of particular types of activity by private entities. This can include utilities such as gas, electricity and water. Rate regulation can have a significant impact on both the timing and amount of an entity's revenue.

IFRS does not provide any specific guidance for rate-regulated activities. The IASB has a project to consider the broad issues of rate regulation and a discussion paper on this subject was imminent at the time of going to press. Pending the outcome of this comprehensive rate-regulated activities project, the IASB decided to develop IFRS 14 as an interim measure.

IFRS 14 permits first-time adopters to continue to recognise amounts related to rate regulation in accordance with their previous GAAP requirements when they adopt IFRS. However, to enhance comparability with entities that already apply IFRS and do not recognise such amounts, the standard requires that the effect of rate regulation must be presented separately from other items. An entity that already presents IFRS financial statements is not eligible to apply the standard.

IFRS 14 is effective from 1 January 2016; however, early application is permitted.

EFFECTIVE DATE OF IFRS 9 LIKELY TO BE DELAYED UNTIL 2018

The IASB has tentatively decided to require entities to apply IFRS 9 *Financial Instruments* for annual periods beginning on or after 1 January 2018.

This isn't the first time that the effective date of this much-debated new standard has been delayed. It had originally been slated to come into effect in 2013, but this was pushed back to 2015 when it became apparent that the project to replace IAS 39 was going to take a lot longer than originally anticipated. But as the IASB and their US counterparts struggled to find a converged solution, it soon became apparent that even 2015 was too ambitious a target.

The end, however, is finally in sight. The new general hedging model – which is discussed further on pages 10 and 11 – was published late in 2013 and at the time of going to press we understand that the chapters on classification and measurement and on impairment are imminent. The board has therefore tentatively decided that IFRS 9 will be effective in 2018; a whole decade since the onset of the financial crisis that resulted in the clamour for IAS 39 to be replaced. And people say the world of standard-setting is slow-paced!

There may, however, be a further twist in the tale as before IFRS 9 can be adopted in Europe, the new standard will need endorsing by the EU. This will be by no means a straightforward process. The debate could be lively.

LUCIANO LOZANO / IKON

NARROW-SCOPE AMENDMENTS

STANDARD	PROPOSED AMENDMENT	DETAILS
IFRS 11 *Joint Arrangements*	Acquisition of an Interest in a Joint Operation.	New guidance on accounting for the acquisition of an interest in a joint operation that constitutes a business.
IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*	Clarification of Acceptable Methods of Depreciation and Amortisation.	Prohibits revenue-based depreciation methods and generally presumes that such methods are an inappropriate basis for amortising intangible assets.
IAS 28 *Investments in Associates and Joint Ventures*	Equity Method: Share of Other Net Asset Changes.	New guidance on the application of the equity method.
IAS 41 *Agriculture*	Bearer Plants.	Bearer plants are now accounted for by IAS 16 rather than IAS 41, permitting the use of either the cost or revaluation model rather than just the latter.
IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures*	Accounting for the Sale or Contribution of Assets between an Investor and its Associate or Joint Venture.	Addresses the acknowledged inconsistency between the requirements in IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is contributed to an associate or a joint venture.

A number of narrow-scope amendments have either been finalised in recent months, or are expected to be completed soon (see table above).

A number of exposure drafts have also been issued proposing further narrow-scope amendments. These include proposals to amend IAS 1 *Presentation of Financial Statements* that are designed to help alleviate some of the problems that have been identified with disclosure in financial reporting.

The IASB has tentatively decided that IFRS 9 will be effective in 2018; a whole decade since the onset of the financial crisis

Eddy James
is a technical manager in the faculty

LEASING UPDATE

One of the beauties of the English language is that words come and go, writes **Peter Hogarth**. Who knew what a 'selfie' was a few years ago? Now they are everywhere. I would now like to make my bid for fame by inventing my own word: 'condivergence'.

The IASB and FASB began their redeliberations of the 'converged' leasing project in March 2014, but while they agreed that all leases (other than those eligible for scope exceptions) should be recognised on the lessee's balance sheet, they could not agree on how they should be reflected in the income statement.

The IASB decided to pursue a single approach for all leases with the lessee accounting for all leases as 'Type A' leases. This would result in a front-loaded expense for all leases, similar to finance lease accounting today.

The FASB decided to pursue a dual approach with classification as 'Type A' or 'Type B' based on the current dividing line in IAS 17. The income statement for Type A leases would be the same as under the IASB's approach. But the income statement for Type B leases would reflect straight-line expense recognition, similar to operating leases today.

As for lessor accounting, neither board showed any appetite to move away from the current IAS 17 model. However, it is interesting that the FASB has decided to put a constraint on the recognition of selling profit or revenue for sales-type leases based on the guidance in the recently published converged revenue recognition standard. The IASB did not agree to such an overlay.

So we have a converged balance sheet and divergent income statement: hence 'condivergence'.

Peter Hogarth
is a partner at PwC

Hot off the press – the IASB's new revenue recognition standard

Phil Barden looks at some potential impacts of the IASB's new revenue recognition standard

The IASB's long-awaited new standard on revenue recognition, IFRS 15, was finally issued in late May. It has been developed jointly with the US standard-setter, the FASB, and is almost completely converged, with only small differences between the two versions of the standard.

The project was added to the IASB's agenda back in June 2002, so why has it taken such a long time to get a standard out? The answer is that it has been necessary to solve a lot of difficult issues of principle - such as unbundling and contingent consideration, to name just two. Previously, the IFRS literature did not adequately address many of these difficult issues, whereas US GAAP tended to address them on an industry-by-industry basis, without necessarily being consistent between different industries. This is the first time that either standard-setter has issued a comprehensive, principles-based standard that applies across virtually all industries.

However, this means that we can expect some teething problems. When companies start to apply the new standard in practice, they will, no doubt, find some ambiguities and perhaps some flaws. The IASB and FASB are anticipating this, and they intend that a Joint Transition Resource Group will examine some of these problems as and when they arise.

The standard is effective for periods beginning on or after 1 January 2017, which might sound too far off to worry about, but the reason for granting such a long implementation period is that some companies will need all of that time to get ready. If you fall into that category, you will want to know now, not later - so it is well worth engaging with the standard soon to assess how much it will affect you.

Although the extent of the impact will vary from company to company, broadly speaking the standard will have two different types of impact:

- It may change the timing of recognition of revenue and profit. For some companies, this will be dramatic; for others, the effects will be smaller. Nevertheless, all companies will need to work through the standard to identify and quantify any changes; and
- It may require changes to processes and systems to enable figures to be produced and reported. Some requirements - such as allocating total revenues between the different deliverables in a contract - may need to be dealt with on a contract-by-contract basis, and that could prove a significant logistical challenge for companies with a very large number of different contracts. Moreover, revenue disclosures are likely to be significantly more extensive under the new standard, and some changes to current processes may be needed to enable them to be produced.

There is far too much new and detailed guidance in the standard to attempt to summarise it here, but three significant areas of change are highlighted below:

- The new guidance on unbundling could significantly alter practice for some entities. For example, if a software licence is supplied together with subsequent services, revenue might be recognised separately for the licence or it might be recognised in combination with the service element as the services are provided, depending on the circumstances.
- Will revenue be recognised at a point in time or over time? The new standard takes a different approach from current IFRSs, and this will change the accounting for some companies. Taking contract manufacturing as an example, revenue might either be recognised at the point of delivery or over the period of manufacture - with the answer being very dependent on the nature of the item manufactured and on the contractual terms.
- Most costs associated with obtaining a contract will have to be expensed, but some of these costs (eg, success fees paid to agents) will have to be capitalised. Practice is diverse at present, and for some companies these amounts can be large.

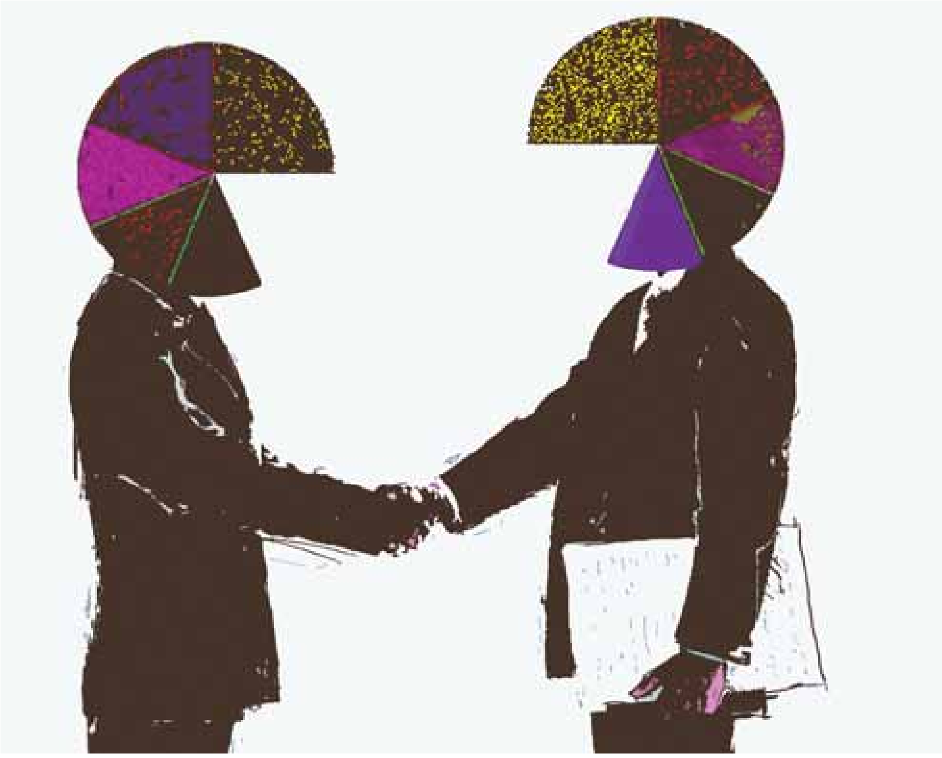
Look out for more detailed coverage of the new standard in the next edition of *By All Accounts*

Phil Barden is a partner in Deloitte's UK technical department

GALLERYSTOCK

Spot the difference

Danielle Stewart looks at the IASB's proposals to update the IFRS for SMEs and outlines ICAEW's thoughts on them



GARY WATERS / IKON

In October 2013, the IASB published an exposure draft of proposed amendments to the IFRS for SMEs. Although the UK does not apply the standard directly, it was important for ICAEW to comment on the proposals because the new UK GAAP is based largely upon it. Moreover, any significant changes to the international document might eventually make their way into UK GAAP.

The proposals were the product of a period of research and outreach by the IASB. Many varied views were expressed to them, not least by their own SME Implementation Group. However, the exposure draft ultimately proposed few changes to the existing version of the standard.

There is only one major amendment, which is to the section on income taxes. This section was originally drafted when a now-defunct exposure draft of changes to IAS 12 was being aired by IASB, with the effect that the requirements relating to income taxes have always been inconsistent with full IFRS. The proposed new section is based on IAS 12, and while it could ideally have included more simplifications, we are broadly satisfied that it is appropriate.

Although there are 57 potential changes in total, some are repetitive and many are minor clarifications that have little real impact. We agree with the majority of the proposed changes, but believe that additional improvements to the standard could have been made (see panel).

CONCLUSION

On balance, we are content with the 'minimal change' strategy adopted by the IASB, because the IFRS for SMEs is primarily aimed at the less developed (from an accounting point of view) nations, so the impact of change to them will only be extra cost, with no perceptible value arising. Nonetheless, the IASB could have made it clearer from the outset it was only tinkering with the standard, because this would have managed respondents' expectations more effectively.

AREAS FOR IMPROVEMENT

1 We think that the IASB should have taken this opportunity to set out some clear principles for future updates of the IFRS for SMEs. Although decisions can be made about incorporating new IFRSs on a case by case basis, we believe that the board should explicitly set out the criteria against which their assessment will be made.

2 The proposals add four new 'undue cost and effort' exemptions, and although there is some new guidance on the use of the exemption, it is not particularly clear or helpful. We have suggested that this guidance should be improved – specifically that the IASB should clarify how entities might assess the balance between costs and benefits and also add some guidance to help auditors assess whether an entity is entitled to apply the exemption.

3 Our preparations in the UK for the introduction of FRS 102 have brought to light some problems with the financial instruments section of that standard, which originate from the same section of the IFRS for SMEs. Most inappropriately, certain instruments which would intuitively be considered 'basic' by most people – and which are treated as such by full IFRS – are classified as 'other' financial instruments by the IFRS for SMEs and therefore have to be measured at fair value through profit or loss rather than at amortised cost. We have suggested that the IASB should correct this anomaly by following the suggested solution currently being exposed by the FRC in the UK.

Danielle Stewart is Baker Tilly's head of financial reporting and chairs the working party that drafted ICAEW's response to the IASB's proposals

THE END IS NIGH

As the new UK GAAP's effective date of 1 January 2015 draws ever nearer, **Jenny Carter** explains that the final pieces of the puzzle are now falling into place

Our work on the new UK GAAP has continued apace in recent months and I'm pleased to say that the finishing line really is in sight now.

FRS 103 INSURANCE CONTRACTS

In March 2014 we issued a fourth new UK GAAP standard - FRS 103 *Insurance Contracts* - which is applicable to all entities that issue insurance contracts. FRS 103 allows entities, generally, to continue with their current accounting practices for insurance contracts. We expect this standard to be an interim solution that will be reviewed in a few years' time to consider whether revisions are desirable in response to regulatory or international accounting developments.

FINANCIAL INSTRUMENTS

When we issued FRS 102 we noted that we expected to revisit its hedge accounting requirements prior to its effective date, once the IASB had completed its work on the topic. As a result we issued FRED 51 *Draft Amendments to FRS 102 - Hedge accounting* in November 2013. The comment period has now closed and we are considering the responses we have received.

FRED 51 aimed to allow entities to apply hedge accounting when this reflects their risk management strategies, without onerous conditions. Respondents generally agreed with the thrust of the proposals, but one area where they have asked us to look again is the transitional provisions. As the transition date for many first-time adopters of FRS 102 will have passed before the amendments have been finalised, it will be important to provide suitable transitional provisions, particularly as many entities will not have formally applied hedge accounting before, despite having entered into hedges for risk management purposes.

We also issued FRED 54 *Draft Amendments to FRS 102 - Basic financial instruments* in February 2014 in response to feedback that the conditions for determining whether a financial instrument was basic, or not, were too restrictive, resulting in too many financial instruments being measured at fair value. FRED 54 proposes amending FRS 102 to allow a wider range of debt instruments to be measured at amortised cost where this is a relevant measurement basis. This should reduce the costs of compliance with FRS 102.

We are aiming to finalise both the amendments to FRS 102 resulting from these proposals by the end of July 2014.

While we previously indicated that we would revisit the requirements of FRS 102 on impairment of financial assets, we are not now intending to make any changes in relation to this prior to the standard's effective date.

RESPONDING TO FEEDBACK ON IMPLEMENTATION OF FRS 102

FRS 102 was generally well received, but as entities and their auditors have been preparing to apply it in practice we have received feedback on a number of points, some of which have necessitated action outside the intended three-yearly review cycle.

We have issued six editorial amendments and clarification statements in relation to FRS 102 in recent months, covering issues such as:

- presentation requirements for financial instruments when an entity chooses to apply the recognition and measurement provisions of IAS 39 or IFRS 9 and/or IAS 39;
- net investment hedges of foreign operations that are branches;
- deferred tax arising on a business combination; and
- transitional exemptions in relation to accounting for service concession arrangements.

GETTY

For ease of use, a compendium of these changes can be found on our website.

STAFF EDUCATION NOTES

We have issued a number of *Staff Education Notes* too. These are intended to highlight certain differences and similarities between FRS 102 and current accounting standards. While they are not a definitive statement on the application of FRS 102, they may be useful when considering transition to the new standard.

FRS 101 REDUCED DISCLOSURE FRAMEWORK

FRS 101 allows qualifying entities to apply EU-adopted IFRS with reduced disclosures. Therefore, when the IASB issues new or revised standards, we must review FRS 101 to maintain the appropriate level of reduced disclosures.

We issued the results of our first annual review in FRED 53 *Draft Amendments to FRS 101 (2013/14)*, which proposed amendments in relation to recoverable amount disclosures and investment entities.

The comment period has now closed and we are considering the responses we have received, with the intention of issuing the amendments by the end of July 2014.

OTHER AREAS OF WORK

In addition to the projects discussed above, we are also considering the likely implications for accounting standards arising from the implementation in the UK of the new EU Accounting Directive. In April 2014 we issued amendments to the FRSSE to reflect the new micro-entities regime. The implications for accounting by small companies are considered in Stephanie Henshaw's article on page 18.

Jenny Carter is project director, codes & standards division, at the UK Financial Reporting Council

VIEW FROM THE FACULTY

TIME FOR SOME STABILITY?

While some changes to FRS 102 were inevitable, **Sarah Porthouse** believes that now is the time to create a truly stable platform.

When FRS 102 was issued in early 2013, it was not expected – at least in the short term – to be subject to significant amendments. The aim was for the new standard to serve as a 'stable platform' so that companies could get to grips with the new regime and effectively plan for their transition.

However, given the significance of the change – it is, after all, a complete overhaul of UK GAAP – it is perhaps unsurprising that it has been necessary to make some amendments in advance of the 1 January 2015 effective date.

Few would argue that the recent amendments proposed by the FRC have not been necessary. Introducing a more principles-based approach to hedging not only brings UK GAAP closer to the new IFRS approach, but also facilitates more meaningful and understandable accounting and disclosure. Moreover, without the proposals to re-draw the dividing line between 'basic' and 'other' financial instruments, many debt instruments would have been accounted for in an inappropriate manner.

So, where do we go from here? There are bound to be new challenges and issues that arise as companies get down to the detail of applying the new UK GAAP – and not just in the more complex areas such as financial instruments. However, for FRS 102 to be a truly 'stable platform', the FRC must take care when it comes to proposing further amendments. In my view, unless it is absolutely necessary, the FRC should now wait as originally intended until its first triennial review before it considers further tinkering with FRS 102.

And let us not forget that the next big change is looming large on the horizon – the implementation of the new EU Accounting Directive. This is going to bring major changes to small company reporting in the UK, not least because it regulates the content of small company accounts. The FRC is certainly going to have its hands full over the coming months as it deliberates on what this will mean for the future of the FRSSE.

Sarah Porthouse is a technical manager in the faculty

Where now for the FRSSE?

Stephanie Henshaw ponders what the future holds for the many smaller UK entities that currently use the FRSSE

The FRC recently announced a major project to review the Financial Reporting Standard for Smaller Entities (FRSSE), expressing the tentative view that the standard should be withdrawn. Given that the FRSSE might be regarded as one of the success stories for accounting standards over the last 20 years, why the call to withdraw it now?

GENESIS

Let's go back 20 years, to 1994, to the genesis of the separate reporting regime for small companies. Simplified company law disclosures for small companies were a relatively recent invention but, with a couple of exceptions, there were no similar exemptions from compliance with accounting standards. The introduction at that time of the new FRSs presented considerable challenges for small companies. I was a CPD presenter at the time and can still recall delegates' consternation at the very idea of 'discontinued activities' and 'historical cost profits and losses'.

A lively debate about whether small companies should apply 'big GAAP' or 'small GAAP' culminated in 1997 with the issue of the first FRSSE and the establishment of the principle that, while small companies should apply broadly the same recognition and measurement rules as large ones, their disclosure obligations should be simpler and the standard they apply should reflect their lack of complicated transactions.

BETTER QUALITY FINANCIAL REPORTING

But not everyone embraced the FRSSE immediately; some accountants decided they did not want to 'learn a second set of rules' and stuck to SSAPs, FRSs and UITF Abstracts, while many others opted for the 'single standard' approach.

When Companies Act requirements were brought into the FRSSE to make it a genuine 'one-stop shop' for small company accounts and again when thresholds rose, so did the number of FRSSE users. As UK GAAP converged with IFRS, FRSSE users were exempted from the measurement rules for share-based payments, providing small companies with another incentive to switch from full UK standards.

So, the FRSSE became a valuable component of the financial reporting landscape in the UK. There may even be an argument that focusing on relevant small company issues without the distraction of 'big company' topics contributed to better quality financial reporting.

A NEW LANDSCAPE

Now that landscape is changing. The biggest companies have been using IFRS for almost a decade now and the UK's new reduced disclosure framework effectively allows their subsidiaries to join them. At the same time, a much simpler disclosure regime has been introduced for micro-entities which is potentially available to a significant portion of current FRSSE users. Most recently, the EU Accounting Directive introduced a statutory limit on small company disclosures, not only reducing the specified requirements, but also preventing member states from adding further disclosures. In addition, the new UK GAAP – which is effective from 1 January 2015 – applies recognition, measurement and presentation rules that are not currently reflected in the FRSSE (eg, deferred tax on revaluations, investment properties), so the transition from small to non-small accounts could be fiddly. Whatever happens, the FRSSE cannot stay as it is.

WHERE NEXT?

The new UK GAAP is a very different proposition from the SSAPs, FRSs and UITF Abstracts that triggered the creation of the FRSSE. It is a single standard (like the FRSSE), shorter than old GAAP, based on consistent principles, and aligns UK accounting more closely with IFRS, although with less complexity. Some may find IFRS terminology jarring, and interpreting a less-detailed standard can be challenging for those not familiar with international standards, but the new regime is coherent and accessible.

FRS 102 doesn't incorporate Companies Act form and content, so – unlike the FRSSE – it isn't a 'one-stop shop'. But those preparing true and fair accounts for non-corporate entities won't be entitled to make use of the micros regime or company disclosure exemptions, so any revised FRSSE would either have to exclude them or include provisions not applicable to companies at the risk of confusing users. With change inevitable, what is the best solution? Let the debate commence.

Stephanie Henshaw is technical standards partner for Francis Clark LLP and chair of the faculty board

CORBIS

TWO STEPS FORWARD, ONE STEP BACK?

Kathryn Cearns asks whether the UK's new strategic report is beginning to improve the quality of narrative reporting

ANDREW BAKER / IKON

The accepted wisdom is that companies' increasingly long and complex financial statements need to be accompanied by clear narrative explanations that provide both additional insights about - among other things - the future of the business and clarity about past performance. However, the front section of annual reports can often come across as a ragbag of various statements and reports with no unifying theme, partly as a result of an accumulation of requirements over time from a variety of sources (including company law, listing rules and governance requirements).

REARRANGING THE DECKCHAIRS

The UK government sought to provide a vehicle for more focused discussion through a new mandatory strategic report. While the legal requirements are to some extent rearranging the deckchairs (many of the requirements were previously in the business review within the directors' report), the government and the FRC have made it clear that they expect companies to use this change as an opportunity to rethink and improve their narrative reporting. New rules on disclosure of gender diversity across companies, greenhouse gas emissions and human rights policies have potentially expanded the volume of disclosures.

The first listed company strategic reports are now out, so it is timely to review what companies are doing.

DIFFERING VIEWS

The first point is that there appears to be substantial variation in application of the legal requirements, which may derive from a lack of clarity about the underlying policy drivers. Companies are taking different views on whether the strategic report has to be separate from the directors' report or not, and whether and to what extent it is acceptable to have information elsewhere in the annual report and cross-refer to it from the strategic report.

In addition, companies have taken different views on how much they should be paring back information to the truly 'strategic', removing clutter and streamlining their reports. Undoubtedly some were already very good reporters; some have made valiant attempts to change things. However, others have done little beyond bare compliance, although sometimes this reflects other pressures they happen to be under.

It is fair to suggest that companies which have tried to change things more radically have found that there is only a certain amount that can be achieved at the first attempt; shareholders and regulators may need to be patient to allow a staged improvement. In addition, the FRC's guidance on the strategic report is only out in draft at the time of going to press, with final guidance expected in June 2014. It may be that the clearer direction and suggestions for best practice that will come with the final guidance will cause companies to think again about whether they can constructively do more.

HUMAN RIGHTS

On human rights disclosures, many companies are at least indicating that they are thinking about their human rights policies and disclosure will follow accordingly, so again this is a work in progress. The gender reporting requirements have caused some confusion, but it looks like this is being overcome (although it would be preferable to amend the legislation at some point to make this meaningful). Disclosures about greenhouse gas emissions have caused some difficulty around the reporting boundary, but again companies are getting there.

IS IT ALL WORTH IT?

Companies are finding, in my experience, that the pain of moving to a much more 'strategic' approach is accompanied by a realisation that once this is accomplished, their reporting process may be much more straightforward in future. But it will be up to the market to reward companies that go the extra mile on their reporting by more analyst coverage, better press comment and - in the end - a lower cost of capital. Only then will companies see that the time and effort has been worth their while.

Kathryn Cearns is consultant accountant at Herbert Smith Freehills LLP and chair of ICAEW's Financial Reporting Committee

From compliance to communication

Paul Druckman explains how he believes the advent of integrated reporting will change the face of corporate reporting

"<IR> is more than a simple disclosure tool: it can help to drive management decision-making by embedding integrated thinking"

Over the next 10 years the shape of corporate reporting will change. This prediction is based on four years of leading the International Integrated Reporting Council (IIRC) which, in December 2013, released the *International <IR> Framework*. The framework was informed by the experiences of the 104 businesses in our pilot programme – including global leaders such as PepsiCo, Unilever, China Light & Power and SAP.

UNLOCKING VALUE

Integrated reporting – or <IR> – aims to unlock value and release benefits to businesses such as lower capital costs, a longer-term investor base and improved performance. It will create a more cohesive reporting landscape, where businesses more effectively articulate their strategy and in a concise way explain how value is created over the short, medium and long term.

The IIRC is supported by the financial reporting community, including accounting bodies and standard-setters. Last year the IIRC and IASB signed a memorandum of understanding to deepen our joint commitment to improve the relevance and value of corporate reporting, a key element of which are the financial statements.

The faculty's members will be familiar with the criticisms of today's financial reporting levelled by businesses and investors alike: that it is too complex and voluminous, that it focuses on technical detail at the expense of the bigger picture, and that it is disconnected from the strategy of the business. Investors, in particular, complain that material information can often be found in the notes to the accounts, obscured by less relevant information.

<IR> will make financial reporting more relevant and turn compliance into communication.

Investors will be able to view the financial statements in context and through the eyes of management. <IR> should also bring about greater consistency between financial and narrative reporting. By linking strategic information about value to the financial report this will strengthen the quality and consistency of the information communicated to the market. <IR> will also improve risk disclosures by ensuring that principal financial and non-financial risks are reported in an interconnected way, reflecting their interdependencies.

INNOVATION

<IR> has moved out of the innovation phase since the release of the <IR> Framework at the end of 2013 and is now in what it calls the early adopter phase. South Africa has been the trailblazer, and since 2010 <IR> has been required by the Johannesburg Stock Exchange on a comply-or-explain basis. One of the key lessons is that <IR> is more than a simple disclosure tool: it can help to drive management decision-making by embedding integrated thinking. As South African telecoms company Vodacom's 2011 integrated report stated: "For us, Integrated Reporting has not been a skin-deep, box-ticking exercise. It has really helped us manage our business better".

<IR> is also a journey that takes several reporting cycles, rather than something businesses can adopt overnight. Koichi Kaneda, senior director at the Japanese company Takeda Pharmaceuticals, said they began with "combined" reporting, before they started to apply the connectivity of information principle which has been a major driver of integration.

MARKET-LED CHANGE

Our aim is to bring about market-led change and we estimate that around 1,000 businesses globally have adopted at least some of the principles of <IR> within their reporting processes. Securities regulators and stock exchanges are also encouraging businesses to improve the quality of disclosures, recognising the importance of information as a driver of better business decision-making and financial stability.

Legislation, too, is leading to a renewed focus by company boards on reporting and how internal decision-making can trigger board discussions that otherwise might not occur. For example, many UK-listed businesses are looking to apply the framework as part of the

MATT KENYON / IKON

process of adopting the legislative requirement to produce a strategic report.

We encourage businesses to consider sector-specific issues and methods to help drive forward <IR>. The IIRC set up the first of these sector groups on banking and finance late in 2013 in an initiative led by DBS Bank in Singapore.

The market response, both to the development of the framework, and now, since its release, has been remarkable and the momentum for change is building. Corporate reporting should aim to reveal, not obscure, strategic information. <IR> is the global catalyst to bring this about.

Paul Druckman is chief executive officer of the IIRC and an ICAEW past president

VIEW FROM THE FACULTY

A potential catalyst for real improvement

Nigel Sleigh-Johnson provides an ICAEW assessment of the International <IR> Framework

Integrated Reporting is increasingly raised in debates in the UK and beyond about the future of corporate reporting, a remarkable success story for the fledgling IIRC and for its ubiquitous CEO, Paul Druckman.

ICAEW has consistently supported the principle of Integrated Reporting during the development of the IIRC's framework. We believe it could act as a catalyst for real improvement in corporate reporting and for the adoption of sustainable business practices.

The framework envisages that an integrated report would be 'either a standalone report or be included as a distinguishable... part of another report or communication.' This flexibility was a key recommendation of ICAEW when commenting on draft iterations of the framework. While some companies will produce a standalone integrated report, as originally envisaged by the IIRC, the UK may want to build on the legal requirement for a strategic report, which should take companies a long way towards meeting the key objectives of the framework.

Rather than make compliance with the framework a mandatory requirement, ICAEW envisages a flexible and voluntary approach, which may well differ among different jurisdictions, from industry to industry and company to company. Embedding requirements in law or regulation is likely to result in a compliance-based product which is anodyne and defensive. Similarly, calls for more detailed guidance for preparers should generally be resisted: an approach grounded in principles and judgement rather than detailed requirements seems likely to work best.

Many organisations are active in this area, mainly major listed companies, but much remains to be done to achieve integrated reporting as envisaged by the IIRC. For example:

- Efforts by the IIRC to engage with mainstream investors will need to be intensified.
- The experience of the IIRC's pilot programme companies will need to be distilled and disseminated as they apply the framework for the first time.
- For UK companies, clarification of the overlap between the requirement for a strategic report and the key aspects of the framework would be helpful.
- The governance and due process of the IIRC will need to be reviewed, in consultation with stakeholders.
- The question of assurance will need consideration.

The next phase is likely to be make or break for the IIRC. ICAEW will remain closely involved.

Nigel Sleigh-Johnson is head of the Financial Reporting Faculty

All progress depends on the unreasonable man

Bob Humphreys makes the case for an international standard for financial reporting in the not-for-profit sector

George Bernard Shaw once argued that: "The reasonable man adapts himself to the world; the unreasonable one persists in trying to adapt the world to himself. Therefore all progress depends on the unreasonable man."

The accountancy profession is the epitome of reasonableness. We have standards, but allow alternative approaches. We have requirements, but allow exceptions. We go to great lengths to differentiate between 'must', 'should' and 'may', and to accommodate sectors, interest groups and countries who like to do things their own way. But ultimately it takes an 'unreasonable' group of people to say: "We're done with adapting ourselves to our surroundings, let's change things."

DIVERSITY

The not-for-profit sector is a classic example of where a diversity of accounting practice has grown up over many years. Until relatively recently UK charities had *carte blanche* to prepare accounts on almost whatever basis they liked. Although the situation has improved immeasurably as a result of successive SORPs, supported by the Charities Acts, we have tended to adapt existing accounting practices rather than seeking out new ways of doing things.

Even when IFRS came peeking over the horizon, we reassured ourselves that we could adapt it to our requirements. Our accounts are meant to make us accountable: yet at a time when everyone is migrating to global standards, we are left with a very parochial and inconsistent framework for reporting our activities.

APPETITE FOR CHANGE

A couple of years ago the proverbial group of unreasonable people came together to see what could be done to improve things. An excellent start was made by conducting a very thorough study of the landscape, the results of which were published earlier this year. The feedback was unequivocal, with 72% of respondents wanting to see an international reporting standard for the not-for-profit sector.

There's obviously a real appetite based not only on the arguments of quality and consistency, but also on saving money by reducing the need to produce different reports for different donors. In the longer term, once you impose greater comparability of accounts, then it will be easier for donors, supporters, partner organisations and beneficiaries to identify inefficient or uneconomic organisations.

POTENTIAL PITFALLS

Despite this overwhelming vote of support for the concept, there are many potential pitfalls. It is far from clear which body should sponsor the development of such a standard, for one.

My vote is for this project to build on its successful start and to keep the current momentum going. The next step should be to get this issue firmly on the agenda of the CCAB and IASB and make it clear that the not-for-profit sector is done with being reasonable.

Bob Humphreys
is Oxfam's
Finance Director

THE CCAB STUDY

In February 2014, the CCAB published the results of its international study into financial reporting by not-for-profit organisations (see **bit.ly/1lXBDya**). The study assessed the need and demand for stronger financial standards. The research was based on an extensive review and an online survey, which received over 600 responses from 179 countries.

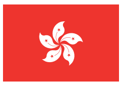
Overall there is strong interest in some sort of international standard for financial reporting in the sector, albeit less so in the UK, and the CCAB has called for more research into what an international standard for financial reporting in the not-for-profit sector could look like.

For more information, please contact nigel.sleigh-johnson@icaew.com

MARCUS BUTT / IKON

International round up

The latest news from key jurisdictions around the world



HONG KONG: NEW COMPANIES ORDINANCE BITES

On 3 March 2014, Hong Kong's new Companies Ordinance (CO) came into force. The majority of the changes for HK-incorporated companies' financial statements take effect for financial years ending on or after 31 March 2015. However, the abolition of nominal (or par) value for all shares on 3 March means a change to March 2014 balance sheets; share capital, share premium account and capital redemption reserve are amalgamated into a single number for share capital.

The new CO eliminates its predecessor's accounting-related disclosures, but mandates compliance with Hong Kong accounting standards. In consolidated financial statements, the company balance sheet is relegated to a note, although it must retain its format and be supported by a note detailing movements on the company's reserves. Private companies with up to HK$200m of turnover and total assets and 100 or less employees can qualify for 'simplified reporting' provided they have 75 percent member approval and none object; automatic qualification is provided for small private companies at a HK$100m threshold.

Mainland China companies listed on the Stock Exchange of Hong Kong will be affected when the Listing Rules are updated for disclosures equivalent to those required by the new CO.

Nigel Dealy is a director in accounting consulting services at PwC in Hong Kong

CYPRUS: TIME TO INTRODUCE THE IFRS FOR SMEs

The IAS Regulation requires European listed companies to prepare their consolidated financial statements on the basis of IFRS as adopted by the EU, and gives member states the option of extending this requirement to non-listed and non-consolidated financial statements.

Since 2007, Cypriot law has required all registered companies to prepare their financial statements in accordance with IFRS as adopted by the EU. This makes Cyprus one of the few countries with a single-tier financial reporting framework; its only GAAP is IFRS as adopted by the EU.

However, in July 2009, the IASB issued the *IFRS for SMEs*, aimed at small and medium-sized private companies. Although the EU Commission has not adopted this standard, six EU countries allow it in one form or another.

As an international business centre with the majority of companies being SMEs, Cyprus needs to introduce a more flexible approach.

The forthcoming changes in the EU Accounting Directive give Cyprus the opportunity to introduce a new two-tier framework. This would not only reduce unnecessary burden but also enhance the reliability, relevance and usefulness of smaller entities' financial statements. Logically this second-tier GAAP should be based on the *IFRS for SMEs*, as adjusted to accord with the new EU Accounting Directive. It's time to create a 'Cyprus GAAP for SMEs'.

Gabriel Onisiforou is an assurance and advisory services partner at EY Cyprus

SINGAPORE: STRENGTHENING THE QUALITY OF FINANCIAL REPORTING

As part of efforts to enhance Singapore's financial reporting eco-system, the Accounting and Corporate Regulatory Authority (ACRA) and the Institute of Singapore Chartered Accountants (ISCA) signed a Memorandum of Understanding (MoU) in January 2014 that will see a public-private collaboration aimed at increasing the breadth and depth of Singapore's financial reporting surveillance regime and strengthen the quality of financial reporting by companies.

By tapping into the expertise and experience of ISCA's Financial Statement Review Committee - which comprises senior practitioners from the accountancy sector - ACRA is now able to expand its financial reporting surveillance programme to a larger pool of companies and their directors. The MoU applies to the review of financial statements with a financial year ended from 1 January 2013.

ISCA will be holding its flagship event, the Singapore Accountancy Convention, in July 2014. The Convention - which will feature luminaries such as IASB chairman Hans Hoogervorst and ICAEW executive director Robert Hodgkinson - will discuss developments and issues impacting the profession internationally and in the region in the key disciplines of accounting, auditing and assurance, ethics and integrated reporting, including the conceptual framework, revenue recognition, leases, financial instruments, fair value measurement and consolidation.

Benjamin Oh is a manager in the ISCA technical standards development and advisory team

STRONGER TOGETHER

Thomas J Linsmeier outlines the FASB's new approach to international convergence

In 2002, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) committed to work together to converge and improve US Generally Accepted Accounting Principles (GAAP) and International Financial Reporting Standards (IFRS).

Since then, the boards have made significant progress in improving and converging their standards, including issuing guidance on business combinations, non-controlling interests, fair value measurements, borrowing costs, segmental reporting and – more recently – revenue recognition. These changes have moved us further along the path toward realising a system of truly comparable accounting standards to the benefit of users of financial statements around the globe.

Twelve years later, the bilateral working relationship between the FASB and the IASB is changing. In its place, we at the FASB envisage a long-term, global standard-setting environment in which the FASB, the IASB and other major capital market standard-setters work as peers, co-operating to facilitate comparability of standards around the world. This multi-lateral model, while not centralised on a single standard-setter or set of standards, is consistent with the goal of promoting greater consistency in global financial reporting while also addressing the specific needs of the individual capital markets that these organisations serve.

We believe the FASB can successfully carry out its mission of improving US GAAP while at the same time seeking to improve and converge financial reporting internationally. Working together, we can create a new path forward in the quest for more common and comparable global financial reporting standards in three primary ways:

1 Through the development of US GAAP

The FASB's primary objective is promoting the reporting of highly relevant information for financial statement users of companies using US GAAP. The FASB will continue to undertake improvements to our standards when necessary to meet the needs of investors and other users of companies preparing US GAAP reports both within and outside the United States. This would include an evaluation of IFRS when implementing improvements to US GAAP. Any improvements that the FASB makes to our standards may also influence the shape and future direction of IFRS.

2 By enhancing relationships and communications with other standard-setters

The FASB's effort to improve US GAAP will benefit from the additional international input resulting from its interactions with the IASB, the International Forum of Accounting Standard Setters, and other national and regional standard-setting bodies. As a result, the FASB will continue to maintain and strengthen its existing co-operative relationships with other standard-setters to promote the broader flow of information and ideas. That will contribute to an environment that fosters greater convergence. In some cases, the need to serve the best interests of investors and other users in an individual capital market may outweigh the goal of creating completely converged accounting standards. But following this path, if committed to collectively around the world, would enable the FASB to work co-operatively with the IASB and standard-setters of other major capital markets toward the goal of agreeing on and adopting standards that either are converged or that have the fewest possible differences.

3 By actively participating in the development of IFRS

Finally, the FASB will advance the development of IFRS by actively providing input on IASB projects through its membership on the Accounting Standards Advisory Forum and through other means. The FASB will contribute to the development of IFRS by sharing views developed through the FASB's due process, stakeholder outreach, analysis and deliberations.

By working together, I believe we can continue to move forward, perhaps in a more achievable way, towards more common and comparable global financial reporting standards.

Thomas J Linsmeier is a FASB board member. The views expressed are his own

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From the faculties

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GET ENGAGED

AUDIT & BEYOND

Engagement quality control reviews (EQCR) are commonly thought to only concern larger firms, but sole practitioners and small firms could find their audit work equally benefits from them. This is because all audit firms must comply with the requirements of the International Standard on Quality Control 1 (ISQC 1).

The Audit & Assurance Faculty recently hosted a webinar explaining that ISQC 1 requires every audit firm to establish and maintain a system of quality control. This must include policies and procedures that address quality control.

Some smaller audit firms may believe (mistakenly) that the EQCR only concerns larger firms because ISQC 1 mandates them for all listed entity audits, making them compulsory for a subset of UK firms.

Possible reasons for an EQCR include the need to consider a familiarity threat, for example, if an engagement partner has been acting for an audit entity for more than 10 years. A firm might decide an EQCR is appropriate if there are going concern issues. "The EQCR is to protect yourself against the possibility that a riskier audit might bring with it more problems," explains Gill Spaul, technical director at Moore Stephens Europe.

EQCRs must be conducted by an appropriate person. They must have the right skills, experience and authority, and should be selected by the engagement partner.

For more from the Audit & Assurance Faculty, visit icaew.com/aaf

RISING IN THE EAST

CORPORATE FINANCIER

With a GDP in excess of $20trn (£11.7trn) and covering 30% of the world's land mass, Asia could well be private equity's promised land.

The domination by family and former state-owned enterprises make the private equity model of active ownership, alignment of interest, medium-term investment horizons and balance sheet optimisation perfectly suited to the restructuring of Asia Inc.

There have already been successes, such as CVC Capital Partners, GIC and the Riady family's $870m (£512m) investment in Indonesian retailer Matahari Department Stores (MDS) in 2010. But buy-out funds have been accused of using a blanket approach to 'Asia'. "Each country's macro, socioeconomic and political landscape is different, and so our approach to ownership and investment must be tailored to each individual market," says Terence Lee, director of KKR in Singapore.

Private equity in the Asia-Pacific region remains a tiny proportion of GDP, and while theoretical demand for private equity finance is huge, it has yet to translate into opportunities on the ground. "We try our best to originate our deals from our own research and proprietary networks," says Lee. "Sourcing deals on a proprietary basis is not only helpful for valuation, but in many cases it makes the post-investment relationship stronger, because the management teams have had the time to get to know us."

For more from the Corporate Finance Faculty, visit icaew.com/cff

COSTLY MISTAKES, QUICK SUCCESSION

FS FOCUS

When planning for the succession of a business, it is important to get a cross option agreement in place to ensure surviving business owners retain company control and the estate of the deceased receives fair value.

But a significant number of businesses do not have such a plan. Many business owners do not realise that they can avoid unnecessary inheritance tax (IHT) by using their will to gift their business assets into a business relief (BR) trust.

Cross options need careful preparation by experienced professionals. Only a bespoke document can cater to specific requirements: do the clients want both a 'put and call' or, in the case of critical illness, just a 'put' option? Where some of the shareholders are married couples, are the shares to pass to the spouse or to the other shareholders? And having ensured a proper cross option agreement has been prepared, what about appropriate trusts in wills to protect BR?

A trust can offer protection against many threats, including IHT. The surviving spouse can have full access during his or her lifetime. The inclusion of a BR trust in a will provides a potential saving of IHT of £400,000 on a shareholding worth £1m, and possibly more as the money is passed down the generations.

A properly prepared share/partnership protection arrangement, with the backing of BR trusts, is simply good housekeeping.

For more from the Financial Services Faculty, visit icaew.com/fsf

And finally...

A BLUFFER'S GUIDE TO BITCOINS

In recent months you've probably heard quite a lot about Bitcoin. But if you can make neither head nor tail of the world's leading cryptocurrency, look no further, as our cut out and keep beginner's guide will tell you nearly everything you need to know to bluff your way through a tricky conversation with an IT geek.

YOU'VE LOST ME ALREADY, WHAT IS A CRYPTOCURRENCY?

A cryptocurrency is a digital medium of exchange that uses cryptography for security. Bitcoins - which were launched by the mysterious Satoshi Nakamoto in 2009 - are the original and best known cryptocurrency. They are, however, by no means the only show in town as a number of rivals, including Peercoin and Litecoin, are also jostling for attention.

SO BITCOINS ARE REALLY JUST AN ELECTRONIC CURRENCY?

Yes and no. Although Bitcoins are now accepted by a growing number of online traders and can increasingly be used to buy goods and services, they do differ from conventional currencies in a number of key ways. Most importantly, as Bitcoins are not issued by any central authority, they are theoretically immune from government interference. While a government can affect the value of its currency through controlling the money supply, it is not possible to interfere with the amount of cryptocurrency in the system as only a prior defined - and publicly known - amount is produced each day.

WHAT DO YOU MEAN BY 'PRODUCED'?

Bitcoins are produced by a method known as 'mining' in which computers use processing power to solve difficult equations. Whoever solves the puzzle has 'mined' a new block of Bitcoins.

SO WHAT HAPPENS ONCE I HAVE MINED SOME BITCOINS?

The Bitcoins are sent to your electronic wallet. This basically stores a string of letters and numbers that are the key to your Bitcoins. You can then either hang on to them in the hope that their value will rise, swap them for a 'fiat' currency using one of the burgeoning number of online exchanges or simply use them to buy stuff. Believe it or not, some pubs are now accepting Bitcoins in exchange for beer! But be careful, if you lose your electronic wallet - for example if your computer is stolen - you're in trouble, as you also lose the keys to your Bitcoins.

WHY BOTHER USING BITCOINS?

Transacting in Bitcoins is fast and cheap. With no banks involved in the process, fees are low or non-existent. Critics would also say that there are significant risks attached at present and that the difficulty in tracing transactions back to individuals makes Bitcoin the ideal medium of exchange for those looking to engage in nefarious activities.

WHAT IS ONE BITCOIN WORTH?

Since prices are based on supply and demand, the rate at which a cryptocurrency can be exchanged for another currency can fluctuate widely. In November 2013, the value of each Bitcoin peaked at $1,250 but this crashed to less than $500 the following month after China restricted trading in the cryptocurrency. But by early 2014 the price had climbed back over $1,000, only for it to plummet once more after the implosion of the Mt. Gox Bitcoin exchange which somehow managed to misplace 850,000 Bitcoins (worth nearly $500m). At the time of going to press, a Bitcoin is worth around $450.

HOW WOULD I ACCOUNT FOR BITCOINS?

That's a tricky question. There's currently no guidance on accounting for cryptocurrencies so your guess is as good as any. They don't seem to meet the definition of cash or cash equivalents and they're probably not a financial instrument either. In fact, they're probably more akin to something like gold (which, of course, is also mined) so perhaps they should be simply carried at cost less any impairment. If the explosive growth of cryptocurrencies continues, perhaps the standard-setters will have to start giving the matter some serious thought in due course.