ICAEW FINANCIAL REPORTING FACULTY

JULY 2013

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BY ALL ACCOUNTS

"PREPARERS NEED TO ENSURE THE GOING CONCERN BASIS OF ACCOUNTING STILL APPLIES" P31

Passing the baton
Meet the faculty's new chair Stephanie Henshaw

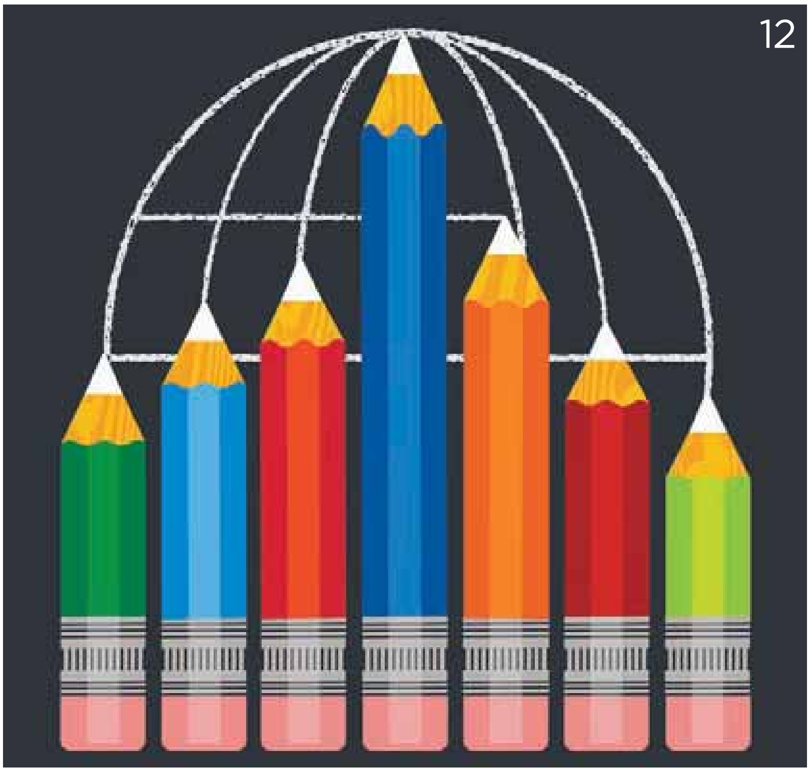
At the finish line
Will the decade-long wait for the new UK GAAP be worth it?

Changing climate
Understanding the new disclosure rules on emissions

Stuck in traffic
Will IFRS ever be a truly global set of standards?

Contents

July 2013



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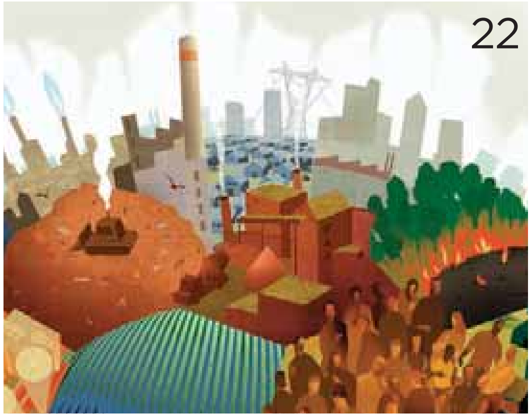

"I'm hoping my background will stand me in good stead as we take on board the new UK GAAP"

Stephanie Henshaw the Financial Reporting Faculty's new chair

7

At the crossroads…

FINANCIAL REPORTING FACULTY

The world of financial reporting is at an important crossroads. Recently, much has been achieved,

but significant challenges lie ahead. IFRS have spread across the globe until today well over 100 countries adopt the standards issued by the IASB or have aligned their domestic standards closely to them. But progress has slowed in the wake of the financial crisis as the United States continues to procrastinate on when, or indeed if, it will join the IFRS community. Moreover, the era of convergence - which has brought many benefits - is quite rightly drawing to a close. So where do we go from here?

Michel Prada, chairman of the IFRS Foundation, may just have some of the answers. I'm sure you'll find our interview with him a fascinating and enlightening read. The faculty too has views on what is needed to cement the future of IFRS. These were outlined in our recent thought leadership paper on the subject, and you can read in this issue a summary of what we recommended.

You may think the future of UK financial reporting is a little clearer now the FRC has finally issued the third of the new standards that will replace existing UK GAAP. Alas, life is never that simple. So it should come as no surprise that there are other challenges on the horizon for UK entities - including new narrative reporting regulations, new EU accounting directives and a proposed new regime for UK micro-entities. These are likely to have a significant impact in the years ahead. All are discussed in this issue.

At the same time, the faculty itself is at a crossroads in some ways, with important changes taking place at the top of our governance structure. Stephanie Henshaw has recently been appointed as the faculty's new chair, while Veronica Poole has taken over as chair of our advisory group. Kathryn Cearns remains chair of our Financial Reporting Committee. As the debate continues in Brussels and London about gender diversity, and as the most gender diverse of ICAEW's faculties, we are delighted with this outcome. Indeed, thus far this year is going very well indeed, with almost all members who joined the faculty in 2012 renewing their subscriptions. It looks like we will finish 2013 with record UK and international membership.

Finally, many thanks to those of you who took part in our survey to find out what members think of this flagship biannual journal. The results were highly encouraging, and the overall the message was clear - you want more of the same, with a continued emphasis on the practical implications of technical and regulatory changes alongside plenty of opinion and analysis. Hopefully we'll do just that in this issue.

We're glad members value *By All Accounts*. But we won't rest on our laurels. We intend to continue to improve what we do and warmly welcome further comments and feedback.

Nigel Sleigh-Johnson

Dr Nigel Sleigh-Johnson FCA
Head of Faculty

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FINANCIAL REPORTING FACULTY
Chartered Accountants' Hall
Moorgate Place
London EC2R 6EA UK
+44 (0)20 7920 8533
+44 (0)20 7920 8780
frfac@icaew.com
icaew.com/frf

By All Accounts is produced by Progressive Customer Publishing, 7th Floor
John Carpenter House,
John Carpenter Street
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Advertising enquiries
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Faculty news

ANDY SIMMONDS RETIRES AS FACULTY CHAIR

The faculty AGM was tinged with sadness as Andy Simmonds – chair since the faculty's launch in December 2008 – bid us farewell and handed over the reins to Stephanie Henshaw (profiled on page 7). The faculty has gone from strength to strength under Andy's tutorage and we will miss his guidance and enthusiasm. We wish him well in his retirement as he rides off into the sunset.

However, rest assured, the appointment of Stephanie means that the faculty remains in safe hands. She will be supported by our new vice-chair Kathryn Cearns.

Meanwhile, Matt Blake, HMRC's commissioners' advisory accountant, and Andrew Spooner, leader of Deloitte's Expert Advisory Panel on financial instruments, were appointed to the faculty's board.

SARAH PORTHOUSE APPOINTED AS FACULTY TECHNICAL MANAGER

We'd like to extend a warm welcome to the latest member of the faculty's staff team – Sarah Porthouse, our new technical manager. Sarah – an alumnus of the University of Warwick – joins the faculty in August from Baker Tilly International, where she worked as a quality assurance and technical manager.

Sarah replaces John Boulton who, after three years of sterling work for the faculty, has taken up a new post at Fitch Ratings. We wish John well in his new role.

ALL CHANGE ON THE FACULTY'S ADVISORY GROUP

The faculty AGM on 23 May marked the end of the tenure of Ian Brindle as chair of the faculty's advisory group. Ian, like Andy Simmonds (top left), has been involved with the faculty since the outset, and we're very grateful for his unerring support.

We're delighted to announce that Veronica Poole has been appointed in Ian's place. Veronica – Deloitte's Global IFRS Leader and UK national head of financial reporting – will take charge of 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 also pleased to announce that Robin Freestone (top right) – CFO of multinational publishing and education group Pearson and chairman of the Hundred Group of finance directors – has joined the advisory group.

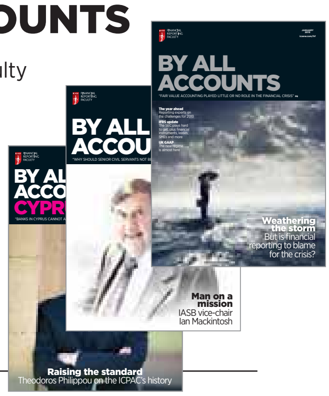
FUTURE OF IFRS REPORT GARNERS RAVE REVIEWS

Since its publication late last year, the faculty's seminal thought leadership paper *The Future of IFRS* has attracted positive feedback from stakeholders and decision-makers worldwide.

You can read more about the paper – which steps back from the hullabaloo caused by the SEC's non-decision on IFRS adoption in the US to discuss what really needs to be done to safeguard the long-term success of the global IFRS project – on pages 12-13. Download a copy of the report from ***icaew.com/futureofifrs***

PRAISE FOR BY ALL ACCOUNTS

ICAEW recently undertook some research into how faculty members regard *By All Accounts*. The results were encouraging. Some 84% of you rated the journal as 'excellent' or 'good' while almost everyone questioned saw it as 'well-written' (97%), 'relevant' (98%) and 'readable' (95%), with 'a good balance of content' (92%). The technical content is also clearly the key to the journal's success – with nearly three-quarters (73%) of you saying you read it primarily as a means of 'keeping technically up-to-date'.



FACULTY EVENTS

INFORMATION FOR BETTER MARKETS CONFERENCE

Our annual Information for Better Markets conference will be on the theme of ‘Reporting financial performance’. It will be held at Chartered Accountants’ Hall on 16-17 December 2013. As well as a team of leading international academics, speakers will include Stephen Cooper of the IASB, Nick Anderson of Henderson Global Investors and Kathryn Cearns of Herbert Smith Freehills, who is also chair of the faculty’s Financial Reporting Committee. Attendance at this major thought leadership event is free of charge.

SIGN UP NOW FOR OUR UK GAAP AND IFRS CONFERENCES

Following the success of our IFRS conference in recent years, the faculty will be holding its inaugural UK GAAP conference at Chartered Accountants’ Hall on 19 November 2013. The conference will provide a comprehensive introduction to the new UK GAAP regime and its implications. Speakers will include Melanie McLaren, the Financial Reporting Council’s executive director of codes and standards, and Matt Blake, HMRC’s commissioners’ advisory accountant.

Meanwhile, our third annual IFRS conference will take place on 2 December 2013. Our keynote speaker will be IASB chairman Hans Hoogervorst. He will be joined by leading speakers from business and the profession as we look at ongoing changes in the world of international financial reporting.

FACULTY READY TO HIT THE ROAD ONCE MORE

Don’t despair if you are unable to make it to London for our conferences this year, as once again the faculty will be taking to the road this autumn. As part of our popular UK roadshow series, we’ll be holding events in cities throughout England and Wales. While many of these events will provide a detailed look at the new UK GAAP regime that will be mandatory for the majority of large and medium-sized UK entities from 2015, we’ll also be running updates on the latest IFRS developments.

MORE CORPORATE MEMBERS JOIN THE FACULTY

We’d like to extend a big thank you to our corporate members, all bar one of whom renewed their faculty membership at the start of 2013. We’re delighted that they are seeing the benefits of being part of a highly-regarded community of professionals at the heart of the financial reporting debate. We’re equally thrilled to welcome a raft of new corporate members so far in 2013, including FTSE 250 constituents Alent plc, Amlin plc and Carpetright plc, life insurer Inter Hannover and top 50 accountancy firms MHA MacIntyre Hudson and Price Bailey.

If you’re interested in joining them as corporate members, contact **Thomas.Gannage-Stewart@icaew.com**

WEBINARS CONTINUE TO PROVE A HIT

The faculty’s regular webinars – which are free to faculty members – are continuing to be popular, especially with those far from London. Our expert presenters provide clear, concise introductions to topical issues. What’s more, viewers have the opportunity to take part in interactive polls and submit questions. They’re a great way to keep up-to-date with developments, regardless of whether you are interested in IFRS or UK GAAP. You can also download the slides and recordings of our webinars afterwards at your convenience.

To find out more about the events on this page visit icaew.com/frfevents or scan the QR code using your mobile device

Keeping it simple

Following her recent appointment as our new chair, **Stephanie Henshaw** spoke to the faculty about her influences, principles and the future

Q What made you want to be an accountant?

A In a way, I'm an accidental accountant, in that I didn't have a particular plan to join the profession. I thought it was all about numbers and I did an English degree. But I met a partner in a Top Ten (as it was then) firm who talked about accountancy so enthusiastically it really sparked my interest. He described it as using communication and analytical skills to solve problems and help businesses develop, with numbers being part of the 'language', and that's how I've always approached it.

I really enjoy the variety of people, problems and businesses that I deal with and get a particular kick out of helping non-accountants understand our 'language' and what it means for them.

Q Who do you currently work for and what is your role?

A I'm currently technical partner at national award-winning Francis Clark LLP, the largest independent practice in the south-west. The firm's awards include mid-tier Auditor of the Year 2011 at the Finance Directors' Excellence Awards.

My role is a mixture of problem-solving, general technical support, compliance and training both accountants and, occasionally, lawyers. I work across the whole firm - not only on financial reporting matters but also auditing, ethical matters, company law and anti-money laundering - and across a range of high-level technical issues and disciplines. I joined the firm in 2008 after 14 years in a similar role at MacIntyre Hudson LLP.

Q Who has had the biggest influence on your career and why?

A There are a number of people who have been important at different stages in my career, because of what I learned from them or how they encouraged me personally. However, my biggest influence was probably my father, a biochemist and expert on penicillin. He believed a career only becomes apparent in retrospect when you see the paths your choices led you down. He was very keen I shouldn't narrow my options and that I should always look for roles that played to my strengths. My career as a technical partner and trainer developed out of that. He was also principled, fair and a master at explaining technical information in a way that was accessible, which is something I have always tried to emulate.

Principles or rules?
Principles
Quality or convergence?
Quality
Beer or wine?
Beer – but it has to be real ale, not fizzy pop!
Town or country?
Both – I need the balance
Glastonbury or Glyndebourne?
Glastonbury – a bit of mud never hurt anyone!

"I hope to bring as much enthusiasm, energy and commitment to the role as Andy"

Q What do you hope to bring to the role of faculty chair?

A Well, Andy Simmonds is a very hard act to follow, but I hope to bring as much enthusiasm, energy and commitment to the role as he has done.

I've been involved with the faculty since it was first mooted and we've come a long way, but I'm keen to expand its membership further. I still meet accountants who don't realise what we offer. I'm also hoping my background will stand me in good stead as we take on board the new UK GAAP.

Q What will be the biggest challenge in your new role as faculty chair?

A Over the next few years there are a number of areas where the faculty will have a big part to play. The introduction of the new UK GAAP from 2015 means supporting our UK members during a potentially challenging transition period. I am confident the faculty will provide a valuable range of resources and be responsive to the practical issues that will inevitably arise. At the same time, more and more jurisdictions are making the switch to IFRS and may look to ICAEW for assistance, so enhancing the faculty's worldwide IFRS credentials continues to be very important.

In charge *of a firm* foundation

The faculty's Nigel Sleigh-Johnson and Eddy James talk to IFRS Foundation chairman, **Michel Prada**

During the final decades of the 20th century, global capital markets changed beyond recognition. Improvements in technology and a growing equity culture meant that it was becoming ever easier to raise capital freely without reference to national borders. It was against this backdrop that the International Organisation of Securities Regulators (IOSCO) gathered in Sydney for its 25th annual conference in May 2000. Recognising that national accounting standards were increasingly becoming an impediment to the free flow of capital, they took a bold decision that would help to kick-start the journey towards a truly global set of standards – it endorsed the use for cross-border listings of the 39 core standards issued by the then part-time International Accounting Standards Committee (IASC). The chairman of IOSCO's key technical committee back then was one Michel Prada.

Fast-forward to the present day and well over 100 countries, including more than two thirds of the G20 nations, require or allow their listed companies to prepare financial statements using IFRS or national standards based closely on them. The IASC has morphed into a truly global standard-setter in the shape of the International Accounting Standards Board (IASB). And overseeing the IASB is the IFRS Foundation – an organisation chaired since early 2012 by the very same Michel Prada.

When we met the erudite 73-year-old Frenchman, he was taking a break between committee meetings at the IFRS Foundation Trustees gathering in London in early April. It was no surprise to hear him refer to himself as a long-term

DOMINICK TYLER

supporter of a globally-accepted, high-quality set of accounting standards. He admits: "I'm not sure that in 2000 I would have bet that a little more than 10 years later all significant markets – including the United States – would require, permit or accept the use of international standards for cross-border listings". But while he talks of the fantastic success of the IFRS project, he also recognises that "outside challenges" have meant that there "seems to have been some slowdown in the trend towards IFRS" in recent years and that there are a number of obstacles that must be overcome.

THE LONG VIEW

"I joined the IFRS Foundation at a difficult time. Some people were blaming accounting standards for exacerbating the financial crisis," Prada explains. "What's more, the lack of clarity on the US position regarding IFRS presented further complications in achieving the G20-endorsed goal of global accounting standards."

But he is adamant that IFRS did not have a significant role to play in causing or prolonging the financial crisis: "I personally do not believe that there is a direct relationship between IFRS and the crisis, and recent academic research backs this up," he says. "Accounting standards try to represent reality – but the reality of the markets at the time was that they were dysfunctional. Therefore, blaming the accounting standards for reflecting that dysfunctionality is like shooting the messenger. There is a collective responsibility about how markets have evolved in the past 10 years or so and it has very little to do with accounting standards."

He is equally unwavering in his view that we should not be overly concerned about the SEC's prevarication over whether or not to allow US domestic registrants to apply IFRS: "Although the US is clearly a major economy, we shouldn't be too worried by these ongoing delays. In my personal opinion, this is purely due to US domestic issues.

"We therefore need to be patient and recognise that the transition period might be longer than we expected initially. But the reality is that this is mainly in the hands of our US friends. We can propose, we can help, but we cannot make decisions on their behalf. Ultimately, we must remember that the G20 has repeatedly confirmed its commitment to IFRS and the US government has signed up to this overall direction."

NEW PRIORITIES

Interestingly, Prada does not see US adoption of IFRS as of immediate importance. Instead, he believes that providing further support in Asia should be the IASB's priority for now. Here, the news is generally more heartening: "The situation in Japan is changing and recent developments are extremely encouraging. The discussions we have with China are very positive. We must remember that their standards are already conceptually very close to IFRS. And Russia has already adopted."

As his focus broadens to the East, Prada believes that the time has come to draw a line under the long-running convergence project with the US standard-setter: "The era of convergence is rightly coming to an end after nearly 11 years of very positive efforts and outcomes. People tend to forget what has been achieved and instead focus on the difficulties that remain. But clearly the system cannot develop on the basis of convergence with the standards of one standard-setter, even if this one

“The era of convergence is rightly coming to an end after nearly 11 years of very positive efforts and outcomes. Clearly the system cannot develop on the basis of convergence with the standards of one standard-setter, even if it is a major one. Now is time to design a new way forwards”

standard-setter is a major one. Now is the time to design a new way forward.”

A MORE MULTI-LATERAL APPROACH

It’s not personal. Other bilateral agreements between the IASB and countries such as Brazil, China and Japan are also being consigned to the history books. Instead, as Prada explains, the IASB is moving towards a more multi-lateral approach. This is manifest in the shape of the nascent Accounting Standards Advisory Forum (ASAF) – a new technical advisory body to the IASB consisting of various members of the global accounting standard-setting community. The inaugural membership of ASAF was finalised in March of this year and its 12 member bodies met for the first time in April. While Prada firmly believes that the IASB already “makes a fantastic effort to listen” through its existing due process and outreach activities, he hopes that the setting up of a single body that brings “many of the big players around one table” will further ensure that the board continues to hear the views of its increasingly diverse constituents.

Importantly, the US standard-setter retains a place at the table, despite calls in some quarters for the US to be excluded from the governance structures of the Foundation until it signs up fully to IFRS. Prada thinks that continuing to work closely with the US is a good thing: “It wouldn’t be reasonable to stop working with one of the major economies in the world. They are both extremely powerful and extremely knowledgeable. I believe we should continue to work together – and ASAF is the perfect forum in which to do just that.”

Prada has high hopes for the new body. “I very much hope that ASAF will be a great success,” he says. “It is not a diplomatic device; it is a working device which will look at technical issues in depth and which I believe will, in time, improve the quality, clarity and credibility of the standard-setting process.”

INVOLVING THE REGULATORS

But the success of the IFRS project is not entirely in the hands of the standard-setters. Once they have been developed, international standards need to be implemented and enforced on a global basis. Enhancing relationships, with not only standard-setters but also regulators, is another important component of IFRS Foundation strategy.

As a former securities regulator himself – he not only served as chairman of the IOSCO Executive and technical committees but also spent 12 years as the chairman of the AMF (Autorité des Marchés Financiers) in his native France – Prada knows very well that it is not the IASB’s job to ensure that its standards are consistently enforced in individual jurisdictions. That is the job of bodies like IOSCO and the European Securities and Markets Authority (ESMA), not to mention the judiciary, and he does not want to tread on their toes.

Prada clearly values securities regulators highly, seeing them as “the frontline of regulation of financial information” and “the first line of defence for investors and users of financial statements”. While he says that the regulators’ job is to “identify issues and deal with them” at a local level, he is keen to emphasise that they also have an important role to play in the global standard-setting process. He tells us that moves are already afoot to enhance co-operation with them in order to enable the standard-setter to “better identify issues raised by implementation, interpretation and feedback”. Doing so can only be another step in the right direction.

Finally, Prada refers to the faculty’s report *The Future of IFRS*, which he commends, and we finish up with a discussion of the various manifestations of complexity in financial reporting, identified in the report as a key challenge for the IASB and its constituents.

A NEW WORLD ORDER

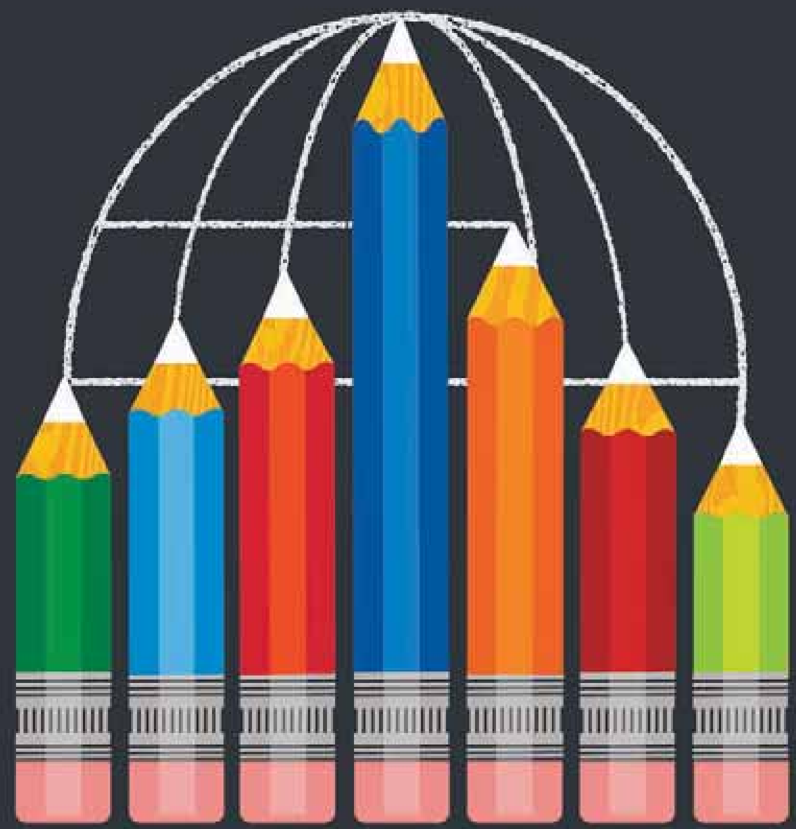
It appears Prada is a man who believes in the vision of a global set of high-quality accounting standards as much today as he did at the turn of the millennium. By moving from the bilateral era of convergence to a more inclusive multi-lateral approach, while strengthening and formalising relationships with regulators, it seems that under his chairmanship the IFRS Foundation is taking positive steps – steps that may ultimately turn the dream of Prada and his fellow IOSCO members into a lasting reality.

It will be interesting to see how things shape up over the second half of his three-year term of office.

Meeting Michel: The faculty’s Eddy James (left) and Nigel Sleigh-Johnson (right) with Michel Prada

The Future of IFRS

The faculty's latest thought leadership report *The Future of IFRS* has attracted a good deal of international attention as stakeholders around the world ponder where the project to create a global set of accounting standards goes from here



GILLIAN BLEASE / IKON

A universal 'financial language' offers many well-documented advantages. Cross-border businesses benefit from reduced preparation costs, and cross-border trading in securities increases as international investors can more readily compare the performance of companies based in different countries.

In turn, it is argued that this results in increased market efficiency and a reduction in the cost of raising capital for companies, which ultimately helps to boost economic growth.

The rapid spread of IFRS around the globe in the past decade means that those benefits are no longer theoretical; a growing body of research shows they are increasingly evident in practice. But momentum has slowed as major projects have stalled and the US and other significant economies have become hesitant as they consider whether or not to commit to IFRS.

Against this backdrop, important questions are now being asked about where the IFRS project goes from here.

At this important juncture the faculty has published a seminal report entitled *The Future of IFRS* that takes stock of the progress made towards developing a global financial language, identifies barriers and challenges that must be overcome if the use of the standards is to continue to spread, and provides recommendations for moving forward.

Regulators worldwide should deliver consistent enforcement, while ensuring that the exercise of professional judgement is not stifled

KEY RECOMMENDATIONS

The report sets out a number of key recommendations including:

Improve G20 leadership

Standard-setters create the standards, but adoption is determined by governments. The G20 should end its calls for convergence and play a more active role in promoting the adoption of IFRS. As a minimum, all listed companies should be given the option of reporting under IFRS.

Get regulators behind IFRS

The IASB needs more active and consistent support from regulators, including IOSCO. Regulators worldwide should collaborate to deliver consistent enforcement, while ensuring that the exercise of professional judgement is not stifled.

End convergence

The 10 years of work to align IFRS with US accounting standards has brought the two sets of standards much closer together. But it's time for the IASB to listen more closely to its other global stakeholders.

Accept less than 100% uniformity

The goal of the IFRS project should be ensuring that financial reporting facilitates international investment and trade by meeting the evolving needs of international investors and businesses, rather than necessarily achieving complete uniformity across the globe.

Minimise complexity

The IASB must remain committed to principles-based standards and simplify its standards wherever possible. The complexity of some IFRS requirements may discourage some countries from fully embracing the standards.

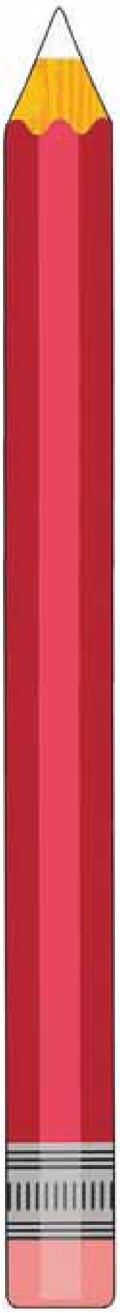
Innovate the IASB institution

The IASB must continue to evolve into a truly global organisation. It must decentralise its responsibilities, experimenting with ways of demonstrating that it is a global body that belongs to and is responsive to its national stakeholders, without embedding inefficiencies or layers of due process that in time might paralyse effective decision-making.

CONCLUSIONS

We stand at an important crossroads. Success is not guaranteed. But if the IASB evolves into the type of organisation we envisage, listening and learning as much as leading, and backed by the G20 governments and the right sort of regulation, we may well in due course look back on the IASB's second and third decades and conclude that they were just as successful - if not more so - than its first.

***The Future of IFRS* is downloadable from: icaew.com/futureofifrs**



WHAT PEOPLE ARE SAYING ABOUT OUR REPORT

The report was both timely and useful in putting a perspective on the past, present and future of IFRS. Well-researched and written, it was at once encouraging, balanced, reflective and strategic.

The strategic directions set out accord quite closely to those currently being pursued by the IASB. We are changing our relationships from bilateral to multilateral as we become truly global. We continue to polish and refine our evidence-gathering and feedback policies. We are trying to make our funding more equitable and independent. We are listening and learning as well as leading. We share the faculty's belief that, while it will not be easy, we will succeed. The need for a global set of accounting standards is too great to contemplate failure. **Ian Mackintosh, IASB vice-chairman**

I should like to congratulate ICAEW on its report *The Future of IFRS,* which I recently spoke about at an ICAEW event in Brussels. Since 2002, the EU has adopted more than 60 regulations transforming IFRS or IFRIC interpretations into EU law and these are applied by 9,000 companies in the EU today. The EU is committed to IFRS. The ICAEW report states that high quality standards are paramount and we see this as vital for the EU. For this reason, Commissioner Barnier has recently appointed Mr Philippe Maystadt as special adviser to provide him with recommendations to enhance the EU's role in promoting high-quality standards. **Didier Millerot, head of unit – accounting and financial reporting, European Commission**

ICAEW continues to be a thought leader on many important financial reporting topics. ICAEW's *The Future of IFRS* report is yet another example of that leadership and is an outstanding reference document for financial professionals around the world. ICAEW continues to bring together policy-makers, academics and professionals in their thoughtful examination of global issues including IFRS. This report contributes in a meaningful way to that ongoing lively debate. **Glenn Tyranski, senior vice president, financial compliance, New York Stock Exchange**

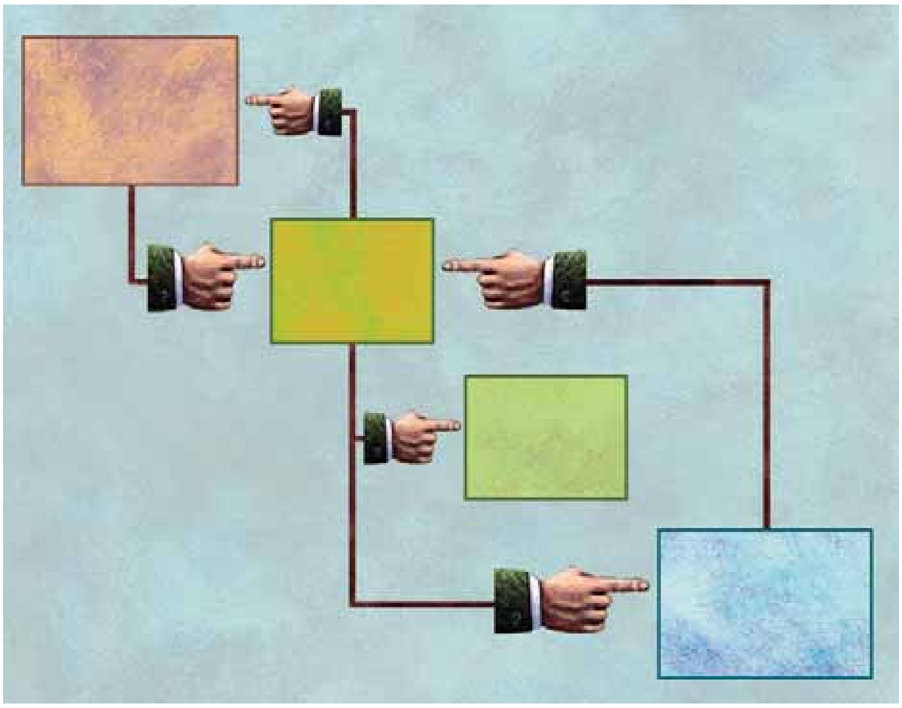
After the IASB has experienced its first setback in 11 years of continuous expansion, EFRAG approves of ICAEW's positive and realistic view of IASB's achievements and next challenges. Thanks to the contributions of our lively European financial reporting community, the European Commission and EFRAG have contributed to many significant improvements in the IFRS Foundation constitution and the IASB standard-setting process that legitimise optimism. The early stages of the IFRS Conceptual Framework debate and the first discussions within the Accounting Standards Advisory Forum illustrate the new era announced by ICAEW and in which Europe is already playing a major role. **Françoise Flores, EFRAG chairman**

The Future of IFRS is a pertinent and timely analysis of the challenges facing the IASB, as we move beyond the convergence agenda, in reaching the ultimate goal of high-quality global standards. As successful as IFRS has been in its first decade, the issues of complexity and disclosure overload resonate with me, as they will with many readers. ICAEW's paper provides an excellent kick-off for the debate. Now it's time to move forward, to work together to restore trust and to make corporate reporting fit for the future. **Mark Vaessen, Global IFRS network leader, KPMG**

Sri Lanka converged with IFRS with effect from January 2012, so we found the contents of ICAEW's report, *The Future of IFRS*, both highly pertinent and extremely useful. We were delighted when ICAEW's Financial Reporting Faculty agreed to host an additional webinar on the report exclusively for our members, CFOs and CEOs. This gave delegates the opportunity to communicate directly with the authors of the report and to better understand the background to current and planned developments in the IFRS world. **Aruna Alwis, chief executive officer / secretary, Institute of Chartered Accountants of Sri Lanka**

A fresh approach

Alan Teixeira considers how the focus of the IASB's technical programme for standard-setting is changing



CORBIS

During 2011 and 2012, the IASB undertook a broad consultation to help us develop our technical work programme. The consultation helped us set priorities and will be repeated every three years. What was very pleasing about this first consultation is that the plans we set out seemed to resonate with the wider IFRS community. There was strong support for us to develop our technical work programme by focusing on three major threads: the *Conceptual Framework*, implementation & maintenance and major projects.

CONCEPTUAL FRAMEWORK

There was almost unanimous support for us to prioritise our work on the *Conceptual Framework* so that we can provide a consistent and practical basis for our standard-setting. We restarted work on this project in September 2012 after a two-year hiatus. An initial discussion paper is expected shortly.

IMPLEMENTATION & MAINTENANCE

Although we are not able to enforce our standards, we are nonetheless responsible for developing standards that are enforceable. We are therefore creating a more responsive implementation programme that includes developing interpretations where appropriate, issuing narrow scope improvements (including annual improvements) and producing educational material. We also see post-implementation reviews as an important part of IFRS maintenance. The first such review, of IFRS 8 *Operating Segments*, is almost complete and we are about to start a similar review of IFRS 3 *Business Combinations*.

MAJOR PROJECTS

I see the reinvigoration of the *Conceptual Framework* project and improvements to our implementation activities as enhancements to our processes. For me, however, the more fundamental changes are in how we will be developing our new major projects.

Our new approach places greater emphasis on defining problems that are brought to our attention as a first step

Every new or amended standard is a solution to a problem. If that problem is not well defined, it becomes more difficult to provide an effective solution. Our new approach therefore places greater emphasis on defining the problems that are brought to our attention as a first step. Identifying there is indeed a problem that warrants fixing is essential. Hence, our research process will include an assessment of whether we should undertake a project to change an existing standard or to develop a new one. After doing so, it is perfectly possible that we might conclude no standards-level project is necessary.

Under this approach, we will develop research papers or discussion papers as the first step in assessing whether an interested party has identified a potential problem that merits the IASB developing a standards-level solution. For each issue, the staff will provide the board with information to help it understand, with evidence, the breadth and depth of the problem. The staff will also provide an assessment of the potential solutions, making a preliminary assessment of the relative costs and benefits of each approach. This could involve the consideration of studies related to that problem or to analogous problems. We might also want to consult preparers and investors on potential solutions so that we can learn more about the potential costs of different options and to identify areas in which investors say that the information they receive now is deficient. This will help the IASB to eliminate choices where the benefits are unlikely to exceed the costs.

Projects will only become standards-level when the IASB is confident that the problem is properly defined and that the staff have identified solutions that are of high quality and are implementable.

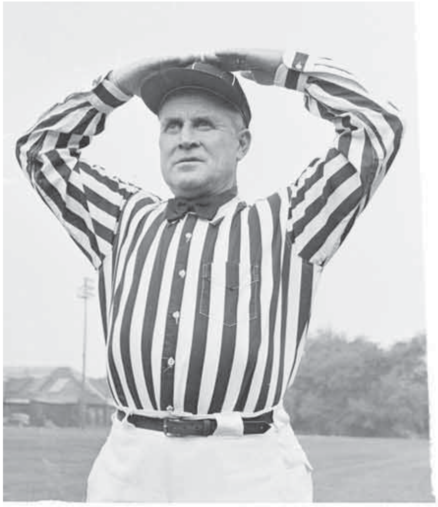
I find this research particularly exciting as it gives us opportunities to involve the wider IFRS community in the initial assessment of financial reporting problems. We plan to involve our network of standard-setting bodies, our network of academic researchers who are interested in IASB activities, and professional bodies, such as ICAEW.

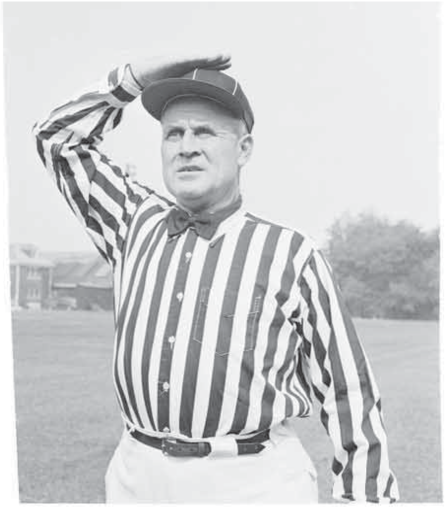
If this process works effectively, once a project is formally added to the IASB's standards-level work plan, the time taken to develop an exposure draft and a standard would be much shorter than it is today.

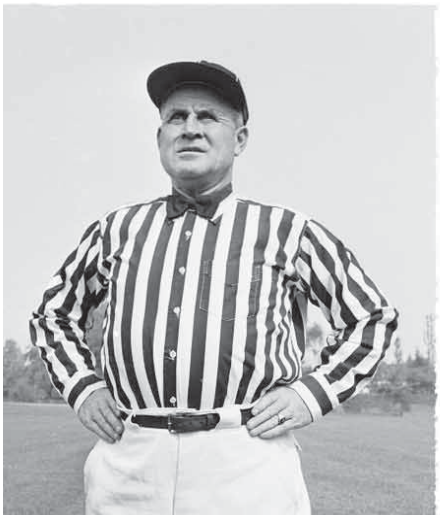
Alan Teixeira is a senior director of technical activities at the IASB

IFRS news

Faculty technical manager **Eddy James** provides a round-up of the latest IFRS developments







CORBIS

RATE-REGULATED ACTIVITIES PROJECT BACK FROM THE DEAD

The IASB's project on 'rate-regulated activities' has sat dormant since 2010 as other issues took precedence in the wake of the financial crisis. But it wasn't forgotten. Indeed, it was a subject that featured highly on the wish lists of many of those who responded to the IASB's recent agenda consultation so, by popular demand, the project is back from the dead.

Rate regulation is widespread and affects industries across many jurisdictions. It typically occurs where a lack of effective competition results in one or more entities having excessive market power that - without constraints - could potentially result in excessive prices being charged for essential goods or services. For example, in the UK, rates are regulated in a variety of industries that were once in public ownership, including energy, water, telecoms and the railways. Globally, there are many different types of scheme. Some define and regulate returns an entity is entitled to generate from its assets, whereas others are designed to subsidise the construction of assets.

Although some national GAAPs provide guidance on rate-regulated activities, there are no equivalent IFRS requirements. Consequently, there is currently diversity in practice. The IASB

NOVATION OF DERIVATIVES

Prompted by the G20's commitment to improving transparency and regulatory oversight of over-the-counter derivatives in an internationally consistent and non-discriminatory way, legislative changes are being made in a number of jurisdictions that would require certain derivatives to be 'novated' to a central counterparty.

Normally in such circumstances, IAS 39 *Financial Instruments: Recognition and Measurement* would require hedge accounting to be discontinued. However, the IASB has issued proposals that would introduce a narrow-scope exception to this requirement where a derivative that has been designated as a hedging instrument is novated to a central counterparty as a consequence of new laws or regulations.

Corresponding requirements are proposed for inclusion in the forthcoming hedge accounting chapter in IFRS 9 *Financial Instruments*.

published an exposure draft on the subject in 2009, but this was shelved in 2010 when it became apparent that there were some fundamental issues that could not be resolved quickly.

The key issue to be addressed is whether assets and liabilities should be recognised where rate regulation results in an entity incurring costs in one period and recovering them in a different period. While some may support this approach, there are concerns that such regulatory assets and liabilities fail to meet the recognition requirements set out in the IASB's *Conceptual Framework*. But the IASB may be able to sidestep this problem as the framework itself is also under review. Indeed, it has hinted that the definitions of assets and liabilities may be changed in order to ensure that regulatory assets and liabilities can be recognised. But doing so may have unintended consequences.

> The definitions of assets and liabilities may be changed in order to ensure that regulatory assets and liabilities can be recognised

Other industries – for example the outsourcing industry – may seek to draw analogies and reach inappropriate conclusions about their own accounting. Moreover, some think that the recognition of regulatory assets and liabilities could result in profit-smoothing.

In April 2013, having re-activated the project, the IASB issued a request for information which asks specific questions about the objectives of rate regulation and how they are reflected in the rate-setting mechanisms employed by rate regulators. By identifying a range of rate-regulatory schemes, the IASB hopes it will be able to determine the scope of its project. The next step in its comprehensive rate-regulated activities project will be a discussion paper later in the year. In the meantime, the IASB has issued an exposure draft – which is open for comment until 4 September 2013 – proposing an interim standard that would allow entities to preserve the existing accounting policies that they have in place for rate-regulated activities with some modifications designed to enhance comparability.

NARROW-SCOPE AMENDMENTS

A summary of other narrow-scope amendments put forward in recent months:

STANDARD	PROPOSED AMENDMENT	DETAILS
IFRS 11 *Joint Arrangements*	Acquisition of an Interest in a Joint Operation	Proposes new guidance on accounting for the acquisition of an interest in a joint operation that constitutes a business
IAS 28 *Investments in Associates and Joint Venture*	Equity Method: Share of Other Net Asset Changes	Proposes new guidance on the application of the equity method
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
IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*	Clarification of Acceptable Methods of Depreciation and Amortisation	Proposes the prohibition of revenue-based depreciation or amortisation methods
IAS 36 *Impairment of Assets*	Recoverable Amounts Disclosures for Non-Financial Assets	Proposes amending IAS 36's disclosure requirements with regard to the measurement of the recoverable amount of impaired assets made as a consequence of issuing IFRS 13 *Fair Value Measurement* in May 2011
IAS 19 *Employee Benefits*	Defined Benefit Plans: Employee Contribution	Proposes additional guidance on the accounting for contributions from employees or third parties set out in the formal terms of a defined benefit plan

WHAT TO EXPECT IN THE SECOND HALF OF 2013

In the next few months the IASB is expected to publish its latest exposure draft on insurance contracts. We're also expecting exposure drafts proposing narrow-scope amendments on topics as diverse as discount rates, bearer biological assets, going concern disclosures, put options and deferred tax.

Discussion papers on macro hedging and the *Conceptual Framework* should also see the light of day before the end of the year. Many of the proposals discussed in this article and elsewhere in this issue are expected to be finalised. So there's plenty to keep us all busy!

LEASES – IT'S HERE!

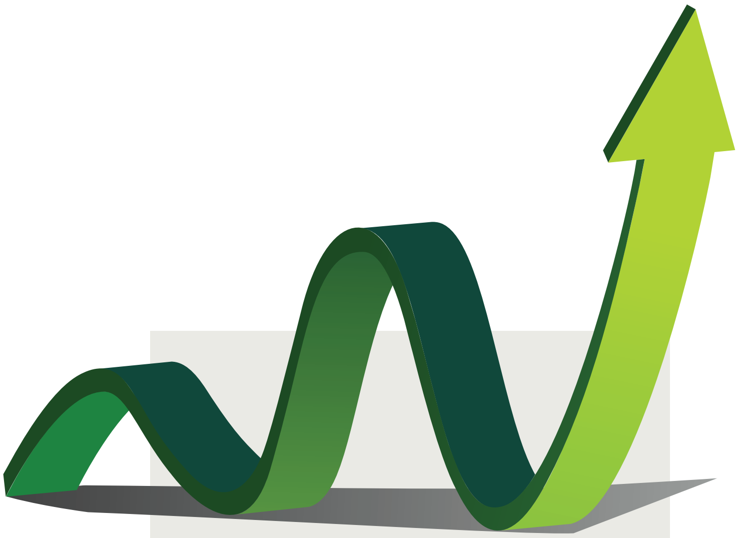
In the previous issue of *By All Accounts* I told you that the IASB and FASB ('the boards') were expected to issue their revised leases exposure draft imminently, writes **Peter Hogarth**. On 16 May it finally appeared – see, I told you so.

The headline remains that lessees will recognise all leases 'on-balance sheet', unless they are considered short-term (ie, their term is less than 12 months) or not leases at all. To answer the obvious question of 'when is a lease not a lease?', you'll need to refer to the exposure draft's new guidance for distinguishing lease contracts from service arrangements. It may mean that some arrangements currently accounted for as leases will not be treated as such in the future.

Much of the focus in recent months has been on establishing the criteria for identifying when expenses and revenues should or shouldn't be recognised on a straight-line basis by lessees and lessors respectively. I talked about this new 'bright line' in my previous article, so won't go over the same ground here. It is worth noting, however, that – coupled with the lease-service boundary mentioned above – it has attracted some sceptical comments, including from the UK's Financial Reporting Council.

So, what next? Comments on the exposure draft are due by 13 September 2013, but we have not yet been given any indication of when the new standard might be effective. As noted by Phil Barden (see box, right), the boards recently decided that the new revenue standard should be effective from 2017, so it is a safe bet that the leases standard will not apply any earlier than that. But whether it might be later – or even a lot later – is anybody's guess.

Peter Hogarth is a partner at PwC



NEW REVENUE STANDARD IMMINENT

The IASB's new standard on revenue recognition is expected very soon, writes **Phil Barden**. For many entities it will be evolutionary rather than revolutionary. Nevertheless, while some entities will need to do no more than enhance their disclosures, others may have to amend their current revenue policies – primarily because the new standard will include detailed requirements and guidance on matters that have in the past been left more to judgement.

It will be worth keeping an eye on the following:

- **Multiple elements** – certain items may no longer be unbundled, which may affect the timing of revenue recognition (eg, software licences).

- **Revenue recognised at a point in time or over time** – a few entities may find the profile of their revenue changes (eg, contract manufacturers).

- **Allocating revenue between elements** – there will be much less room for judgement, which may raise practical challenges for entities with a large number of different contracts.

- **Contract modifications** – new rules will determine whether these are accounted for prospectively or retrospectively, which may create practical challenges where modifications are common and extensive.

- **Contract acquisition costs** – new rules will specify when such costs should be capitalised and when they should be expensed.

The standard is expected to be effective from 2017. But it's not too soon to start planning, particularly if systems changes are needed. In some cases, the timing of recognition of revenue – and hence profits – may change significantly, and that could affect, for example, key performance indicators, tax, cash flows, bonus plans and debt covenants.

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

GREAT EXPECTATIONS

The IASB exposure draft setting out revised proposals for the impairment of financial instruments has finally been published. **Riana Wiesner** considers the implications of the proposed expected loss model

The IASB's latest proposals, issued on 6 March 2013, build upon previous work to develop a more forward-looking impairment model that recognises expected credit losses on a more timely basis. The objective of the proposed model is to mirror as closely as possible the economics of lending activities by reflecting the pattern of deterioration and improvement of credit quality, and distinguishing between financial instruments that have experienced a significant increase in credit risk and those that have not.

Conceptually, initial credit loss expectations are priced into financial instruments - for example, banks charge sub-prime customers higher interest rates to compensate for the higher credit risk that comes with such borrowers. This means these initial loss expectations do not give rise to an economic loss. However, subsequent increases in the credit risk of the borrower do represent an economic loss, because they are not reflected in the pricing. So, ideally, initial estimates of expected credit losses would be reflected by adjusting the effective interest rate and any changes in expected credit losses would be recognised as gains or losses in profit or loss. This is what the IASB proposed in its original exposure draft, published in 2009, but while many respondents felt that this approach had some conceptual merit, they were concerned it was overly complex and was therefore not functional.

OVERVIEW OF THE PROPOSED MODEL

The new exposure draft proposes an expected credit loss model that aims to approximate the information provided by its predecessor in a more cost-effective way. This is achieved by linking the recognition of lifetime expected credit losses to a significant increase in credit risk compared with initial expectations. The proposed model requires a broader range of reasonable and supportable information, including forward-looking information, to be used to determine expected credit losses.

For financial instruments that have not experienced a significant increase in credit risk or that are of high credit quality (such as investment grade), only a portion of

The proposed model requires a broader range of reasonable and supportable information to be used to determine credit losses

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lifetime expected credit losses is recognised. The amount recognised is based on 12-month expected credit losses, and serves as a proxy for adjusting the effective interest rate for the initial expected credit losses. For financial instruments that have experienced a significant increase in credit risk since initial recognition, lifetime expected credit losses are recognised. Expected credit losses are updated at each reporting date to reflect changes in credit quality.

PRACTICAL IMPLICATIONS

The proposed accounting for expected credit losses is based on existing information that is used to manage credit risk. The IASB therefore expects entities to be able to use existing expected credit loss measures, such as some prudential regulatory measures, as a basis for implementing the proposals, both to assess whether lifetime expected credit losses should be recognised and to measure expected credit losses. However, some adjustments are likely to be required, for example, to adjust historical loss experience for future credit loss expectations.

The IASB is aware that the information available to entities and existing systems vary by jurisdiction, entity and type of financial instrument. The exposure draft therefore includes some practical expedients to assist in implementation. One such expedient is the simplified approach for trade receivables and lease receivables, where lifetime expected credit losses can always be recognised. Another relates to financial instruments with low credit risk, such as those that are rated equivalent to investment grade. As long as a financial instrument has a low credit risk, only a 12-month loss allowance is recognised. This means that in both of these cases an entity need not determine whether a significant increase in credit risk has occurred.

The exposure draft further specifies that an entity only needs to consider information that is available without undue cost or effort, and acknowledges that in some cases that information will be 'delinquency information' – there is a rebuttable presumption that significant deterioration occurs when an asset is more than 30 days past due. However, information that is available and is being used in normal credit risk or financial reporting processes cannot be ignored. For example, if an entity uses macro-economic indicators as a qualitative overlay in addition to delinquency information for credit risk management purposes, such information cannot be ignored when estimating expected credit losses in accordance with the proposals.

> The IASB believes that its proposed expected loss model will ensure a more timely recognition of credit losses

IMPROVED TRANSPARENCY

The IASB believes that its proposed expected loss model will ensure a more timely recognition of credit losses than is the case under the current incurred loss model. It also believes that its proposed model better approximates the economic reality of expected credit losses. This should result in more transparent information about an entity's credit risk exposure and about changes in expected credit losses, which will lead to more relevant and useful information for economic decision-making. The IASB further believes that having one impairment model that applies to all financial instruments (including debt instruments measured at fair value through other comprehensive income) is a significant simplification to accounting for financial instruments.

A COMMON SOLUTION?

There are common features between the IASB's proposals and the model proposed by the US standard-setter, the FASB. In both cases, there is no threshold for the recognition of expected credit losses and the information used to measure expected credit losses is the same. For assets that have deteriorated significantly in credit quality since initial recognition and that are below investment grade, the amount of expected credit losses recognised under the two proposals should be the same. The difference is in the measurement of expected credit losses on financial instruments that have not experienced such a deterioration. The FASB proposes that lifetime expected credit losses should also be recognised on those financial instruments. However, the IASB believes that recognising such losses disregards the economic link between pricing and the initial expectations of credit losses.

The IASB and the FASB will both consider the feedback received on their respective proposals and will investigate whether there is common ground on which to move closer to a converged solution.

The comment period for the IASB's exposure draft closed on 5 July 2013.

Riana Wiesner
is a senior technical manager in the IASB's financial instruments team. The views expressed here are her own.

UK GAAP: CLEARED FOR LANDING

Jenny Carter explains that the issue of FRS 102 means a new UK reporting regime almost a decade in the making is approaching the finish line

In March 2013, FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* was issued by the Financial Reporting Council (FRC). As long ago as 2004, it was recognised that there was no case for two wholly different sets of accounting standards – IFRS and UK GAAP – in the medium-term, yet it has taken until now for FRS 102 to be finalised. We think it was worth the wait.

FRS 102 replaces the majority of current UK accounting standards with one accessible and usable document that is only around 10% of its predecessor's length. With a clear index, coherent principles and cross-referencing, this should be an easy standard to read and use. Nonetheless, judgement will still be needed in applying its requirements.

As well as improving the usability of accounting standards, FRS 102 makes some significant changes to accounting requirements and modernises them in line with how businesses have evolved during the last decade. This includes recognising that derivatives and other financial instruments – once the preserve of large multi-nationals – are increasingly used by smaller businesses. Such instruments will be recognised on-balance sheets by entities applying FRS 102.

What FRS 102 means for each specific entity, and whether there will be significant changes in their reported performance, will depend on a number of factors, including whether it has entered into complex financial instruments, whether it is a member of a multi-employer or group pension scheme and whether it has investment properties.

SPECIAL EDITION OF BY ALL ACCOUNTS

Later in 2013 the faculty willl be publishing a special edition of *By All Accounts* focusing on the new UK regime. As you'd expect, it will be packed with detailed analysis not only of the requirements of the new regime but also the practical implications of transitioning to it. With articles from standard-setters and members in business and in practice, we're sure it will be a valuable read.

Other faculty resources
The faculty has also developed a range of other resources to help you get to grips with the new regime. Our factsheets, webinars and the new dedicated section of our website have proved popular with members. If you haven't taken a look at what is on offer, we'd encourage you to do so.

Events
We'll also be holding our inaugural UK GAAP conference in November 2013 and a series of events focusing on the new regime throughout the country as part of our autumn 2013 roadshow series. For more details see the Faculty News section of this issue.

As well as improving the usability of accounting standards, FRS 102 makes changes to accounting requirements and modernises them in line with how businesses have evolved during the last decade

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As a result of the FRC listening to feedback, there are a number of areas where FRS 102 differs from earlier exposure drafts in permitting existing UK accounting practice to continue. For example, revaluations of property, plant and equipment will remain an option, as will the capitalisation of development costs. Moreover, an option has been included to allow entities that manage certain financial instruments on a fair value basis to elect to measure them that way in their financial statements.

Although FRS 102 has been issued, the work on UK accounting standards does not stop here. While the expectation is that FRS 102 will be a stable platform that is reviewed and changed only every three years, we will, however, issue exposure drafts updating some of its financial instruments requirements relating to hedge accounting and impairment of financial assets once the IASB has completed its work in these areas. This will avoid having to wait until the first three-yearly review before making these important changes.

INSURANCE CONTRACTS

We are also developing FRS 103 *Insurance Contracts*, which is already cross-referenced from FRS 102 and will apply to any insurance contracts held by an entity applying the latter standard. It will potentially be relevant to entities other than 'insurers'. An exposure draft is expected to be issued later this summer.

The main objective of FRS 103 is to allow the continuation of existing practice in accounting for insurance contracts in the run up to the more fundamental regulatory reform that lies ahead and the likely publication of a new international accounting standard on insurance contracts. As a result, the changes required to accounting on first-time application of FRS 103 should be minimal, although there may be other changes for insurers resulting from the application of FRS 102.

Entities with insurance contracts should, therefore, not wait for FRS 103 to be published before starting to think about how FRS 102 will affect them. First, FRS 102 includes a definition of an insurance contract, and those entities not previously applying FRS 26 *Financial instruments: recognition and measurement* will need to think about which of their contracts are insurance contracts and which are financial instruments. The latter will be within the scope of sections 11 and 12 of FRS 102. Second, insurers are 'financial institutions' as defined in FRS 102, and there are particular disclosure requirements for such entities in section 34 of FRS 102 which will mean that those not previously applying FRS 26 may need to make additional disclosures.

It is currently intended that FRS 103 will be effective for accounting periods beginning on or after 1 January 2015, which is the same effective date as the other new standards. As this will mean insurers have less time to prepare for the implementation of the new regime than other entities, the FRC will consider the effective date again as it finalises the standard.

WHAT ABOUT THE FRSSE?

At the time of writing, the future of the FRSSE is still in the balance while we await the finalisation of the revised EU Accounting Directives. The FRC has previously promised to consult on the future of the FRSSE once the new legal framework is set.

REDUCED DISCLOSURE FRAMEWORK

Although FRS 102 replaces the majority of current UK accounting standards, it is still part of a small suite of standards. In addition, the FRC has issued FRS 101 *Reduced Disclosure Framework*, which allows entities within its scope largely to apply the recognition and measurement requirements of EU-adopted IFRS while providing reduced disclosures. It builds on the fact that UK accounting standards have previously given disclosure exemptions to subsidiaries, recognising the different users and information needs attached to these financial statements. It should be an efficient choice where group financial statements are prepared in accordance with EU-adopted IFRS, although each group will need to consider its own circumstances in making the choice about which accounting standard to apply.

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

Examining emissions

Richard Spencer and **Lois Guthrie** ask whether the upcoming mandatory disclosure of greenhouse gases by UK companies provides decision-useful information

Subject to parliamentary approval, the UK government will shortly publish regulations requiring the mandatory disclosure of greenhouse gas emissions. This article sets out what we expect the regulations to require, based on the latest draft and discussions we have had. It may be that the final requirements differ.

WHO WILL BE AFFECTED?

Although prompted by the Climate Change Act, the requirement for quoted companies to report greenhouse gas emissions in their directors' report will be included in the Companies Act 2006 (CA 2006) as a result of amendments in the Strategic and Directors' Reports Regulations 2013. Quoted companies here means those that are listed on the main market of the London Stock Exchange, officially listed in the European Economic Area, or admitted to dealing on the New York Stock Exchange or NASDAQ.

Judging by the current draft, the regulations will require companies to report their emissions annually, along with the methodology used to calculate the emissions results, and an intensity ratio. They raise a number of challenges for boards, including dilemmas about the boundaries of what is reported.

BOUNDARIES

Boundaries are imposed to make sense of things; they are artificial borders around organisations and systems that aid understanding by limiting their scope. In the case of the draft regulations, the boundary of greenhouse gas emissions is set by reference to those activities for which the reporting organisation is responsible. Unfortunately, that boundary does not necessarily match the boundary for the strategic and directors' reports, which is set (for group companies) by reference to the undertakings included in the consolidation, which we interpret to mean the financial consolidation. By incorporating the proposed new regulations into CA 2006, the requirements automatically adopt narrower organisational reporting boundaries, based on financial responsibility and financial reporting, than was anticipated by the wider 'responsibility' referred to in the Climate Change Act.

The Carbon Disclosure Project's work shows that the majority of companies report emissions over which they have operational control (whether or not they own the premises, transport or machinery and so on from which greenhouse gases are emitted). So the regulations could well be out of kilter with market practice. In other words, it may be that the regulations impose a boundary that inadvertently limits the amount of information companies will provide and that differs from what is already common practice. They may therefore generate information that isn't likely to be that useful or drive the intended outcomes.

NARRATIVE REPORTING

The second key issue is that in the draft regulations there is no reference to any narrative reporting requirements to make sense of the greenhouse gas footprint and intensity ratio. This will surely leave users scratching their heads and wondering what to make of the data in the absence of any contextual narrative. There is some earlier guidance on this, promulgated by The Department for Environment, Food and Rural Affairs (Defra), and that will no doubt be updated, but it can be ignored by reporting entities.

DECISION-USEFULNESS

We have long argued that new disclosure requirements are welcome if, but only if, they lead to decision-useful information. The right information must go to the right place at the right time if the best-informed decisions are to be made. Along with the leading firms and accountancy bodies, ICAEW has been an active participant of the Climate Disclosure Standards Board's technical working group. The guidance we have developed there has made the case convincingly that a greenhouse gas footprint by itself is not much use. These data need to be linked to an assessment of regulatory and physical risk and to strategy to be meaningful.

It would be a pity if the opportunity is missed to ensure proposed disclosures are truly decision-useful.


Richard Spencer is head of sustainability at ICAEW and **Lois Guthrie** is a director at the Climate Disclosure Standards Board

Cutting clutter

Amanda Swaffield explains that September reporters will lead the way with strategic change in UK narrative reporting

The more an annual report becomes a repository for information requested by policymakers and special interest groups, the more its purpose becomes blurred and the harder it is to draw out its most critical content. Most people would agree we should 'cut the clutter' and that reports should be shorter, more concise and include only company-specific information of relevance to investors.

But is there about to be a step change in the quality of narrative reporting? The Department for Business, Innovation and Skills (BIS) began a project to reinvigorate narrative reporting for all UK companies in 2010. After a further consultation in 2011, the final regulations will be laid before parliament in the near future. The more radical proposals - eg. that most of the directors' report would be online - have been dropped. However, I suspect the discussion over electronic reporting hasn't died and is certainly a topic preparers will be keen to pursue in the future.

If the regulations are approved, 30 September 2013 reporters will be the first to prepare a strategic report in place of the current business review. They will also be the first to apply the 2012 UK Corporate Governance Code, and revised requirements for disclosure of directors' remuneration, which will be laid before parliament soon.

WHAT WILL CHANGE?

All companies, other than small companies, will be required to provide a 'strategic report', which is effectively the content of the current business review (including risks, KPIs and fair review of performance), separately from the directors' report.

Quoted companies will need to describe their strategy, business model and position on gender diversity and human rights. This should link through to financial statements and remuneration of company directors.

The rest of the directors' report will remain largely unchanged for unquoted companies, although a few requirements will be deleted, for example, charitable donations and the creditor payment policy.

Quoted companies will need to include information on greenhouse gas emissions (discussed opposite).

DO THEY GO FAR ENOUGH?

The regulations are part of a wider agenda to improve the transparency and corporate governance of UK companies. And while they are a step forward, they could have gone further. The diversity agenda, for example, is wider than just gender. It is also questionable whether all elements of the strategic report are strategic in nature for all companies. For example, greenhouse gas reporting is likely to be more of a strategic issue for an oil and gas company than, say, diversity. The regulations allow companies to promote information from the directors' report to the strategic report in such cases. But, conversely, there is no option to demote mandatory disclosures in the other direction.

SO WILL THE 'FRONT HALF' OF COMPANIES' ANNUAL REPORTS LOOK DIFFERENT?

In some cases, perhaps not. *Joined up writing* - the Deloitte survey of annual reporting - shows that the quality and integrity of reporting has probably never been higher. Companies preparing concise reports that avoid repetition and communicate as well as comply with the regulations are likely to be good reporters under the new guidelines. Some reporters may take the opportunity to review the existing front half of their annual report and try to reduce overlap by providing one clear narrative that explains how their objectives, business model, strategy, risks and KPIs link together. Others may just pay lip service to the regulations by adding the additional mandatory disclosures.

So what is the benefit? A concise, well thought-out report may reassure investors a company has a clear and well-executed strategy. 'Tidy desk, tidy mind' is a sound adage. Investment in a one-off exercise to simplify the narrative should result in long-term cost savings.

Amanda Swaffield leads Deloitte's narrative reporting team

Keeping micro-businesses in motion

Nigel Sleigh-Johnson reflects on some of the issues raised by recent attempts in the UK to roll back the tide of regulation

In February 2013, the UK Department for Business, Innovation and Skills (BIS) published proposals for simpler financial reporting for micro-entities. The proposals followed on from a decision by the European Union early last year to allow each member state more flexibility in deciding what reporting requirements should apply to the smallest of businesses. The aim of the proposed changes - to reduce regulatory burdens and save micro-businesses money - is laudable.

ECONOMIC PROSPERITY

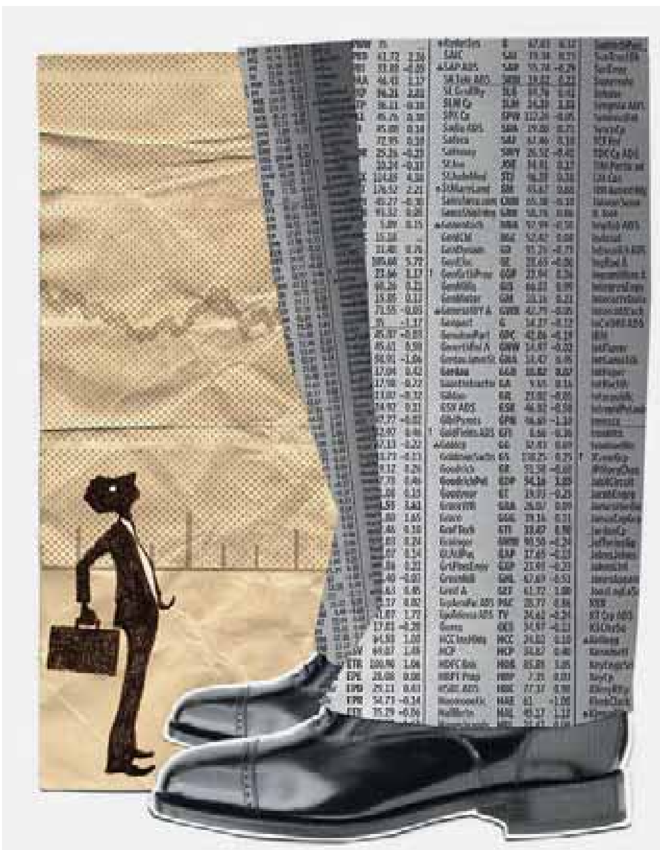
Micro-entities are defined in EU law as those meeting two of the following three requirements: net turnover up to €700,000, gross assets not exceeding €350,000 and no more than 10 employees. The exemptions offered would allow micro-businesses to prepare simpler balance sheets and profit and loss accounts, and to very greatly reduce the amount of disclosure in the notes.

Micro-businesses as a whole, if defined as those with fewer than 10 employees, comprise about 95% of all enterprises in the UK and account for some 32% of all employment. Not only is this a substantial proportion of the UK economy, but also it is in this sector that much of the innovation and entrepreneurial start-up activity - which is essential to economic prosperity - will occur. Unnecessary or unduly onerous regulation can represent a real barrier to these innovative, growing enterprises, stymieing development and distracting management. Such obstructions should, as far as possible, be curtailed. ICAEW is very supportive of the commitment of BIS to explore ways in which regulation for this important sector may be rationalised.

ACCESS TO CREDIT

But it is essential to ensure that initiatives in this area do not have a negative impact on the usefulness of the financial information produced by micro-businesses. Many already find access to credit highly challenging, and it is generally accepted that this is inimical to the economic growth sorely needed in the UK. A radical simplification of the financial reporting of such businesses may, over time, act to exacerbate this problem.

The extension of credit depends on confidence in the counterparty. If lenders and trade creditors have any concerns at all that the information they are presented with may be deficient - for example in relation to related party transactions - or that they will not be able to obtain reliable information during the course of the credit period, they may be less willing to lend or trade on credit. And this won't just be at the margin. Additional information will sometimes be requested by finance providers in these circumstances, albeit at additional cost to the company, but trade counterparties may not be in a position to do so. In any case, such a mechanism is not a complete substitute for readily available and well-understood financial information.



ICAEW'S VIEWS

ICAEW's representation letter therefore concluded that there are fundamental risks in the proposals that hadn't been fully assessed. EU law also allows member states to exempt micro-entities from including certain accruals and prepayments in their accounts, and we voiced particular concerns over the proposed mixing of two different types of accounting - cash and accruals - which may cause confusion and misunderstanding.

We also pointed out that there were several areas the consultation paper didn't cover which require more work, such as the implications for tax compliance and for the determination of distributable profits.

We will continue to try to influence BIS as it drafts regulations over the coming months. It should, after all, be possible to remove disproportionate regulatory requirements in this area without risk to economic growth and the wider UK economy.

Nigel Sleigh-Johnson is head of the Financial Reporting Faculty

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Brussels briefing

Susanna Di Feliciantonio explains that the EU's accounting and financial reporting agenda remains full

Following many months of discussion about the Accounting Directive, member states and MEPs finally struck a deal on 9 April 2013.

Some readers will be disappointed to hear that the 'maximum harmonisation' approach to small company disclosures remains, meaning member states will only be able to require such companies to disclose additional information in very limited circumstances.

However, a number of improvements have made it into the final agreement – including the introduction of an option to use an alternative balance sheet format, a more common sense approach to goodwill, the re-inclusion of merger accounting and the ability for member states to allow the use of fair value principles. The new directive, which as we go to press still needs to be formally adopted by both the European Parliament and Council, also introduces new country-by-country and project-by-project reporting requirements for some companies active in the extractive or logging industries.

The ink on the new directive will not stay dry for long as the European Commission has already proposed amendments designed to enhance transparency around non-financial information provided by companies. Building on an earlier stakeholder consultation, the proposals seek to increase the relevance, consistency and comparability of such data by requiring large companies to disclose non-financial information within their annual reports on a 'comply or explain' basis. Under the proposals, companies can use internationally-accepted frameworks (such as the UN Global Compact or the Global Reporting Initiative) to disclose material information on social and environmental matters. Large listed companies will also be expected to provide details of their diversity policies within their corporate governance statements. It is now for the European Parliament and the Council to decide on the final terms of any legislative changes.

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EVALUATING THE IAS REGULATION

Eight years after the introduction of IFRS for EU listed companies, the European Commission is launching an evaluation of the 2002 IAS Regulation. Speaking at an ICAEW workshop in Brussels earlier this year, Didier Millerot (head of the European Commission's accounting and financial reporting unit) described the initiative as an opportunity "to gain a practical appreciation of the issues across the single market".

THE ROLE OF EFRAG

Meanwhile, Commissioner Michel Barnier has appointed Philippe Maystadt (former President of the European Investment Bank) as special adviser, tasked with considering how to reinforce the EU's contribution to IFRS. Maystadt, who is due to report back in November, will focus his attention on the governance of the European Financial Regulation Advisory Group (EFRAG) and the Accounting Regulatory Committee. He is likely to issue recommendations on how to better integrate differing views internally while ensuring that the EU speaks externally with a single voice.

OTHER ISSUES

Accounting issues also continue to crop up elsewhere. A high-profile European Commission Green Paper on long-term financing, published in March, dedicates some space to the potential impact of accounting principles on investment. Stakeholders are specifically asked, as part of the accompanying public consultation, whether fair value accounting principles have encouraged short-termism in investor behaviour and whether there are alternatives or ways to compensate for such effects.

Public sector accounting standards are also under the spotlight. Another report issued in March – this time by Eurostat, the EU's statistical arm – suggests that while International Public Sector Accounting Standards cannot easily be implemented across the EU, they represent a suitable framework for the future development of European Public Sector Accounting Standards. Echoing some of the current EU debate on IFRS, the report indicates that further clarity will be needed around the EU governance process.

IS THE FINISHING LINE IN SIGHT?

With the 2014 European Parliament elections and subsequent change of leadership at the European Commission in sight, Brussels policymakers are focused on getting to the finishing line on pending laws while exploring issues that may well form the priorities for the next Internal Market Commissioner and newly- or re-appointed MEPs.

Susanna Di Feliciantonio is head of EU public affairs in ICAEW's Europe Region office

AN INCONVENIENT TRUTH?

Brian Singleton-Green defends the much-maligned incurred loss method

As the incurred loss method of measuring impairments of financial assets is about to be consigned to the dustbin of history - apparently to no one's regret - it may seem quixotic to put in a good word for it. But it's a method that's much misunderstood and unfairly defamed, and in the interests of justice, a few words should be said in its defence.

The key point is that the supposed contrast between an expected loss model and an incurred loss model is a false one. All impairment losses are expected losses. They are a measurement of a reduction in expected future receipts. To refer to a reduction in expected future receipts as 'incurred' is to use a word that does not make any sense in this context.

Paragraph 59 of IAS 39 *Financial Instruments: Recognition and Measurement,* states that an impairment loss is incurred "if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset … and that … event … has an impact on the estimated future cash flows of the financial asset". This clarifies that what we are talking about are expected cash flows. The difference between an expected loss approach and an incurred loss approach is therefore not about expected losses - they are both about that - but the evidence to be used in deciding whether a loss should be recognised.

The incurred loss method relies on objective evidence and events subsequent to initial recognition. Both these points seem unexceptionable. The alternative to objective evidence is subjective evidence, which is really no evidence at all - just someone's unsupported opinion. 'Event' is given a very broad meaning - we'll return to this in a moment - and it seems logical that the event should be one that is both past and subsequent to initial recognition. If the event preceded initial recognition, it should have been taken into account in determining the asset's fair value on initial recognition. If the event is in the future, then it's difficult to see what objective evidence for it would be, other than events that have already occurred.

Paragraph 59 also gives examples of what constitutes objective evidence of relevant events. The examples include "national or local economic conditions that correlate with defaults" - which include "an increase in the unemployment rate" and "a decrease in property prices". This is very broad. It should give businesses ample scope, if they consider that loans have become impaired, to find relevant evidence to support recognition of an impairment loss.

In March 2013, the IASB issued an exposure draft setting out its proposed successor to the incurred loss model. The new approach - discussed further on pages 18-19 of this edition - is more forward-looking and, in specified circumstances, would require recognition of impairments even when there is no objective evidence of a credit loss event.

My personal view is that a new approach has been deemed necessary because it seems politically unacceptable to say that financial reporting did not contribute to the financial crisis in some way, and the incurred loss method is a convenient scapegoat. The new approach - sometimes referred to as the 'three buckets' method - may well achieve the accelerated loss recognition that is its intended goal, and it may be a better method than what we have now. But we should not imagine that we are moving from something that is not an expected loss model to something that is. All we are doing is moving to a different type of expected loss method.

Whether it helps prevent future financial crises remains to be seen.

Brian Singleton-Green is a technical manager in the faculty

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Applying judgement: Using the 'true and fair' override

Some boards may wish their financial statements looked rather different. **Kathryn Cearns** asks when it is right for companies to move away from accounting standards and UK company law

Section 393 of the Companies Act 2006 states that a company's directors must not approve their accounts if they do not consider them to be true and fair. This applies regardless of whether those accounts are prepared using UK GAAP or IFRS.

However, what this means in practice continues to be a subject of some debate. As stated in a legal opinion on the meaning of 'true and fair' written by Lord Hoffmann and Dame Mary Arden in 1983: "It is a common feature of such concepts that there is seldom any difficulty in understanding what they mean but frequent controversy over their application or particular facts."

When 'true and fair' was first promulgated in UK - and then EU - law, accounting standards as we know them today were almost non-existent; most generally accepted accounting practice was not even written down. But, importantly, business practices and transactions were also generally more straightforward than they are today.

In today's business world, transactions are not only sophisticated and complex; frequent innovation is also endemic. Accounting standards have struggled to keep up. They have also tended to become ever more detailed and specific. But 'true and fair' has nonetheless remained the touchstone.

A series of legal opinions on true and fair are helpfully grouped together on the UK Financial Reporting Council's website (***bit.ly/XGskXU***). The advent of IFRS led to the most recent update, but the central principles of the original opinion given in 1983 continue to apply, the main point being that 'true and fair' as a legal concept will generally be interpreted by the courts as elucidated in accepted accounting standards.

Care and proper due process are therefore extremely important in standard-setting in order to establish the authority of standards.

The legal opinions make it clear that what is considered 'true and fair' changes over time as accounting and business practices develop. For example the 1983 opinion explains that: "The meaning of true and fair remains as it was in 1947. It is the content ascribed to the concept which has changed" and "... the provisions of the schedule [to the Companies Act] are static whereas the concept of a true and fair view is dynamic." It is clearly vital that accounting does not become atrophied and hence not fit for purpose.

It is, of course, unrealistic to expect accounting standards to cover every situation. Standards recognise that fact by building in a hierarchy of authoritative pronouncements that should be used to assess new or unusual situations where there is no specific standard. In an IFRS context, the relevant guidance is found in IAS 1 *Presentation of Financial Statements*, paragraphs 11-12.

When applying the standards, either directly or according to the IAS 1 hierarchy, produces a counter-intuitive result, the question will generally be whether the relevant

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

transaction or event was contemplated by extant standards. If not, it may be right to depart from the rules, but full disclosure must be given of what the position would have been had the standards been followed (IAS 1.20). Crucially, the combination of the comprehensiveness of the standards, the hierarchy framework, the expected rarity of the need to depart that is written into the standards (IAS 1.19), and legal opinions and case law, means that this does not lead to a 'free-for-all'. Put bluntly, seeking to apply the true and fair override because "I don't like the answer" is not good enough.

The specificity of IFRS and UK standards is variable, but they cover the bulk of usual business transactions.

By definition, overrides of the standards will therefore be rare. Ultimately, each case must be looked at on its merits and judgement exercised in the context of the above framework in order to reach a true and fair view.

Seeking to apply the true and fair override because "I don't like the answer" is not good enough

GARY WATERS/IKON

A servant of two masters

David Damant asks whether one set of financial statements can ever meet the needs of all potential users

The IASB's *Conceptual Framework* clearly states that financial statements are written to enable the users of accounts to make decisions and – crucially – that those decisions are based on a judgement as to the ability of the enterprise to generate future cashflows. And what else except future cashflows is of interest to the capital markets and other users such as employees? But while the financial statements contain much of the evidence on which judgements about the size, timing and certainty of future cashflows can be based, they do not contain the answers.

This is the approach that has been applied by the IASB and its predecessors since inception. However, it does not appear to be known or understood by many of those who are currently calling for IFRS to be simplified or aligned with prudential or other regulations.

CUTTING FOR THE WRONG REASONS

Thus pressure to 'simplify' accounts by reducing disclosures is dangerous if based on the delusion that the figures in the primary financial statements are the answers.

Disclosures are vital if future cashflows are to be judged. The balance sheet valuation of derivatives (which by definition modify future cashflows) is of limited importance as compared with the description of their characteristics, however long those disclosures have to be. Cutting disclosures may mean that decision-making information is lost.

DIFFERENT NEEDS

The main practical consequence of the approach adopted by the IASB is that it simply cannot produce the information required by those who do not seek to use the financial statements to make judgements about future cashflows. This has been accepted for years by the tax authorities who make their own adjustments before levying tax. But this point is now central to the debate about regulation and prudence. Accounts produced for the capital markets contribute to the efficient use of capital. If those accounts are modified by regulatory or prudential requirements, the efficiency with which capital is invested will be qualified.

Investors require neutrality – to show everything as it is, not with prudential provisions to guard against a rainy day. They require fair values – which may not always be appropriate for the calculation of regulatory ratios. Yet in many places, it still is considered that the capital markets and the regulators should use the same accounts. However, much as this may have been true in a simpler past, it is no longer possible to simultaneously serve both masters, as their aims contradict each other.

While the figures relevant to the regulatory process are themselves vitally needed, we must resist the temptation to devise a separate set of accounting standards for banks and other regulated enterprises. Such an approach would lead to conceptual difficulties – especially in the context of consolidated enterprises containing some regulated and some unregulated companies. So what is the solution?

A VERY PRACTICAL DEDUCTION

All that is needed is a separate section of the financial statements in which the regulatory figures can be set out in as much detail as necessary, having been derived from and reconciled to the IFRS figures. Regulators would have all the information they need, and investors would also find this section relevant to their separate analysis of the pure IFRS statements.

David Damant was a board member of the IASC and an independent chair of the IAASB consultative advisory group

GETTY

PAUL JACKSON/IKON

Room at the top table?

Sumita Shah asks whether there is a role for a chief financial officer at the heart of government

The UK faces tough decisions in the coming decade. According to the Office for National Statistics, public sector net debt was £1,161.5bn as at February 2013, equivalent to 73.5% of the country's GDP. As a result, it now seems likely that the deficit reduction programme which began under the coalition government will stretch into the next parliament, and possibly beyond.

The problem is exacerbated by the fact that - as a society - we are living longer. The number of people aged 65 and over is likely to double to 19 million by 2050, resulting in extra demands on health services, social care and pensions.

Within the context of this broader set of challenges, public spending decisions made today will shape tomorrow's public services. ICAEW's recommendations in its policy paper, *A CFO at the Cabinet Table?*, contribute to this debate and provide a means to empower policymakers to shape future services efficiently.

The UK is a global leader in public sector transparency. The Treasury now produces the Whole of Government Accounts, an annual set of consolidated accounts. The National Audit Office scrutinises public spending on behalf of parliament, and the Office for Budget Responsibility provides independent analysis on the state of public finances. To maintain this position, it is important that UK policymakers consider best practice, not only within other governments around the world but also from other sectors. Private sector practice is not without its faults, but it provides some important lessons for the public sector.

The role of the CFO and group finance function provides financial discipline in the business world. While these features of the private sector are no panacea, they have a track record of supporting good financial management and complex organisations. Most global companies would not thrive without a CFO sitting alongside the chief executive within a structure of rigorous accountability to the board.

Regardless of whether an organisation is in the private or public sector, and regardless of whether it is a global business organisation or a government, strong financial disciplines and strong financial leadership is important. In the current environment of stretched public finances, this is more important than ever. Indeed, ICAEW believes that a senior civil servant needs to take responsibility for this financial leadership at the top of government.

In all of this the tone from the top is crucial. The radical changes we propose will require significant leadership and commitment by government ministers. The absence of such change will exacerbate economic instability and uncertainty. Our three-stage reform process will accelerate financial discipline across Whitehall. We are calling on politicians from all UK political parties to:

- Transform the role of the Treasury into a more pro-active finance ministry, enabling it to become a group finance function with a more strategic role not only in providing advice and financial direction to policymakers but also in the implementation and delivery of policy across government. The Treasury needs to be the lead adviser to government on economic, financial and regulatory policy.
- Create a CFO role to head up this group finance function, reporting to the Treasury's permanent secretary and to the cabinet secretary, who then ultimately report to the cabinet. This new CFO would take overall responsibility for financial disciplines across government departments.
- Empower finance directors in government departments and elevate their status to facilitate the embedding of strong financial disciplines and financial leadership across the public sector.

ICAEW's recommendations are framed in a UK context but may well resonate with those involved in government in other jurisdictions. Efficient and effective government demands fiscal transparency, but information alone will not be enough. Strong financial disciplines and leadership, an enabling environment and the pursuit of best practice are also essential.

Sumita Shah is public sector regulatory policy manager at ICAEW

Hong Kong perspective

Nigel Dealy shares his views on recent reporting developments and their implications for companies in Hong Kong and mainland China

The fourth quarter of last year saw the issue of Asia's largest convertible bond of 2012. The proceeds of the Hong Kong Stock Exchange's (HKEx) 0.5% US$500m five-year convertible bond went towards funding its HK$17.3bn acquisition of the London Metal Exchange. That it chose a convertible form of funding reflects their popularity with companies in Mainland China, Hong Kong and the rest of Asia, partly due to the flexibility of the equity-linked market. Printing such a bond also meant less potential dilution for HKEx's existing shareholders. In addition, its terms allowed HKEx to call the paper at 101% of accreted value if it failed to complete the acquisition within six months. It is thought that this is the first time such a clause has been included in an Asian convertible bond.

Stock Exchange Tower in Hong Kong

Clauses such as this one can cause headaches for accountants as they try to fathom the requirements of IAS 32 *Financial Instruments: Presentation*. The question is whether such clauses - and others dealing with, say, 'anti-dilution' adjustments - breach the 'fixed-for-fixed' test that is key to classifying the conversion option as equity. Unnecessary complexity in the drafting of the standard does not add to its ease of use.

Not unexpectedly, regulators in Hong Kong frequently take a close look at how listed companies account for convertibles. For example, in its *Quality Assurance Annual Report* for 2012 (The 2012 Report), the Hong Kong Institute of Certified Public Acountants (HKICPA) commented again on significant application issues identified during its financial statement review programme. The HKICPA is less than impressed.

The 2012 Report - like its 2010 predecessor - included the following findings:

- Embedded redemption options - incorrectly not recognised and measured because 'bondholders were not expected to exercise the option' or 'the issuer did not intend to redeem the bond early';
- Anti-dilution adjustments - inadequately assessed as to whether they achieved their purpose and did not contravene the 'fixed-for-fixed' test;
- Changes to terms and conditions - a lack of understanding as to whether these were inducements for early conversion, or caused repurchase and replacement or merely a modification; and
- Functional currency - not assessing that the functional currency of the issuer differed from the denomination currency of the convertible and thus caused failure of the 'fixed-for-fixed' test.

Perhaps the most concerning point from The 2012 Report is the apparent readiness of some auditors to accept management representations. These included redemption options having no value or that 'adjustments' to conversion price are under the control of management and thus are not relevant to the assessment of compliance with the 'fixed-for-fixed' test. In the current environment, such findings are not helpful to the profession in Hong Kong or the mainland.

Accounting for convertible bonds is not the only controversial aspect of IAS 32. The 2012 IFRIC exposure draft of an interpretation on *Put Options Written on Non-controlling Interests* has provoked much debate, particularly those exercisable at fair value. Such put options are favoured by many mainland companies, which have significant minority investors in their group structures. They believe 'net' accounting under IAS 39 *Financial Instruments: Recognition and Measurement* and the consequent negligible value is appropriate. Suffice to say, IAS 32's 'gross' accounting with the recognition of a redemption liability, whose change in value is recognised in profit or loss, is not liked. The decision of the IFRS Interpretation Committee to refer the issue back to the IASB before finalising the interpretation has created hope for a favourable change.

However, tinkering with IAS 32 is not the answer. Increasingly, IAS 32 is found to be 'not fit for purpose'. The IASB should resurrect the stalled project on financial instruments with characteristics of equity and address the accounting for financial liabilities and equity comprehensively.

WHAT IS THE 'FIXED-FOR-FIXED' TEST?

Under IAS 32's 'fixed-for-fixed' test, a derivative or other contract will qualify for equity classification only where it will be settled by the issuer exchanging a fixed amount of cash or another financial asset for a fixed number of its own equity instruments. Otherwise, the instrument is classified as a financial liability.

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

GETTY IMAGES

A voice for Cyprus

Marios Cosma recently joined EFRAG's Technical Expert Group. Here he highlights some of the issues he plans to focus on as he takes up his new post

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SMALL AND MEDIUM-SIZED ENTITIES

My new role provides me with a great opportunity to input into the development and practical applicability of financial reporting standards from a small European country's perspective. Positions around the proportionality of financial reporting standards in their application to member states are important to advance, especially at a time when the European Union is moving forwards in reducing reporting requirements for small and medium-sized companies.

A reporting framework for companies of small and medium size, such as the IFRS for SMEs, is particularly interesting for Cyprus where the complete set of IFRS is currently applied for companies of all sizes. With the vast majority of entities being of small and medium size and recent developments such as the passing of the EU Accounting Directive, it is important to have an accounting framework for smaller companies that both works and provides the right sources of information.

Adoption of the complete set of IFRS in smaller entities often results in overloading accounting requirements for these entities. Therefore, an accounting framework for smaller entities will be beneficial for the great majority of Cypriot companies.

FINANCIAL INSTRUMENTS

The development of IFRS 9 *Financial Instruments* is also of particular interest to me, as it represents major reform in recognition and valuation of financial assets. In the current environment, with the 'haircut' in Greek government debt (and maybe to other sovereign debts), the impairment calculation is of major significance. It is hoped that the new standard will help the accounting more accurately reflect the economic realities.

The new standard will be applicable to the large number of investment firms, financial institutions and investment holding companies that are registered and operating from within Cyprus. They will have to carefully consider the impact of IFRS 9 not only on their financial reporting but also their accounting procedures. This will no doubt be a challenging exercise for the sector.

> In Cyprus, where – if anything – the economic crisis is broadening, many companies will continue to face going concern problems

Clearly, the recent developments in Cyprus - most notably, the so-called 'bail-in' that resulted in a raid on customer deposits at the country's two major banks - are likely to have material financial reporting implications. For many companies whose financial statements are prepared with a December 2012 year-end, this will mean disclosing a non-adjusting event under IAS 10 *Events after the Reporting Period*. This unique event will require extensive disclosure in the financial statements of a great number of Cypriot and foreign companies that used to keep deposits in these two banks. The disclosures will include an analysis of the event and the estimated loss for each company, increasing the accounting judgement required for this estimation.

GOING CONCERN

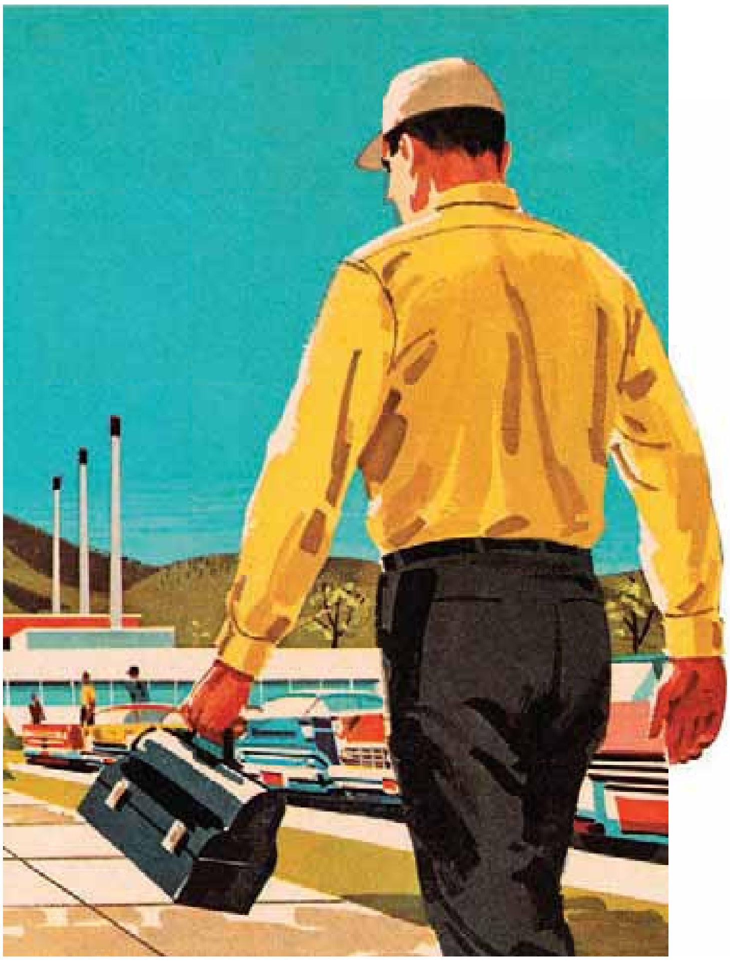
Coupled with the deepening recession predicted for Cyprus and certain other European countries for 2013, preparers need to ensure that the going concern basis of accounting continues to apply. In Cyprus, where - if anything - the economic crisis is broadening, many companies will continue to face going concern problems. These should be appropriately reflected in financial statements. Reference will need to be made to IAS 1 *Presentation of Financial Statements* in order to ensure that the correct basis of preparation is used, as the going concern basis may not be appropriate for some companies. Moreover, even where the going concern basis is appropriate, the material uncertainties arising from the current economic conditions and their impact on the financial performance will need to be properly disclosed by some companies.

Preparers and auditors will need to consider all the economic and political factors so that the users of the financial statements can rely on financial statements to give a true and fair view.

Marios Cosma is director – tax & financial institutions compliance at K. Treppides & Co and a member of EFRAG's Technical Expert Group

TOOLS OF THE TRADE

Marianne Mau provides an overview of the faculty's latest factsheets



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With the recent publication of the three standards which together form the basis of the new financial reporting regime in the UK, it is perhaps inevitable that the first few factsheets for 2013 have had a UK focus.

The first factsheet, *The New UK Regime*, answers frequently asked questions about the new standards and the new system. In particular, it considers how the new UK regime, as outlined in FRS 100 *Application of Financial Reporting Requirements*, will affect reporting entities, what choices are available to them and what considerations might influence that choice. It also considers some of the practical implications of moving to the new framework.

The second factsheet, *Reduced Disclosure Framework*, looks in greater detail at the second standard in the new UK regime, FRS 101, which sets out a reduced disclosure framework available to 'qualifying entities' that otherwise apply the recognition, measurement and disclosure requirements of EU-adopted IFRS when preparing their individual financial statements. This factsheet looks at the exemptions available, other changes that need to be considered, and the transition requirements when moving from EU-adopted IFRS or current UK GAAP to FRS 101.

The third in the series, *The New Financial Reporting Standard*, outlines the key provisions of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. It is anticipated that the majority of large and medium-sized private companies that are currently applying UK GAAP will adopt this new standard. The factsheet identifies the key differences between current UK GAAP and the new standard, and what entities ought to be doing now to ensure that they are ready for the change that lies ahead.

Further factsheets exploring in greater depth some of the challenges presented by the new regime will be published later this year and in 2014. In the meantime, the three new factsheets provide the essential information required to start planning for the changeover in 2015.

It is anticipated that many large private companies currently applying UK GAAP will adopt FRS 102

IFRS

There are several significant new and revised international standards effective for accounting periods beginning in 2013, including major new standards on consolidated financial statements, joint arrangements, disclosure of interests in other entities and fair value measurement and a revised version of IAS 19 *Employee Benefits*. There are also a number of other amendments, interpretations and improvements effective for accounting periods beginning in 2013. Our factsheet, *2013 IFRS Accounts*, provides a guide through these standards.

We regularly update existing factsheets for EU endorsements and significant amendments to the standards to ensure they remain relevant and up-to-date. We have had our own improvements project too, when updating the factsheet *Impairment - Applying IAS 36*. This factsheet now includes more by way of detail and practical tips.

We will be adding further factsheets to the IFRS range as new or modified standards are published by the IASB. In particular, the long-awaited standard on revenue recognition is expected this summer and the faculty is planning a factsheet outlining its key implications once it becomes available.

WHAT NEXT?

We always welcome your views, so if you have any suggestions for future factsheets or comments on those already published, email **frfac@icaew.com**

For a full list of the factsheets published by the faculty, download a copy of *Get the Facts* from **icaew.com/frffactsheets**

Marianne Mau
is a technical manager in the faculty

From the faculties

Keep in touch with our selection from ICAEW's other faculty magazines

FS FOCUS

UNLIKELY BEDFELLOWS

Should private equity (PE) firms get involved in the running of retail banks? Plenty of PE firms are interested – consider the auction of 316 RBS branches, with a long line of PE firms queuing up to enter the bidding.

But their motives still raise suspicions that could scupper their ambitions for greater involvement in the financial services sector.

Despite the tempered reaction to PE buying into retail banks, those within PE can point to recent successes in the financial services sector, including the flotation of insurance broker esure and the improved performance of OneSavings Bank, which was created in 2011.

PE firms say they offer a streamlined structure, which leads to more efficient decision-making and better corporate governance. Obstacles they'll have to overcome include the sheer scale of numbers involved in the infrastructure of running a bank. But some believe PE is just not a good form of ownership for a bank. "PE exists to make profits for a relatively small number of firms and individuals and it does that by identifying short-term opportunities to take undervalued assets, leverage them and maximise the exit value," said Paul Lynam, chief executive of Secure Trust Bank. "That is not the type of philosophy that lends itself to consumer, private or SME banking markets."

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

CHARTECH

HOW APT: CHOOSING THE RIGHT APP

For many, having a company app is considered a must these days. Mobile technology allows businesses to engage and retain customers via apps on smartphones and tablets. Many also use them to support employees in their work.

According to a survey by Strategy Analytics, more than 200 million people will use an app worldwide this year. Over 30% of respondents rated customer relationship management as the mobile app that would help businesses the most, while 13% rated business intelligence, including KPIs and reporting, as the most useful app. But do you need one and what do you need it for?

Richard Cree, group editor of *economia*, says building an app should be thought through: "Some companies feel they need to have an app but they have not worked out what it's for. If you don't have a clear idea it could just run away from you."

Accountancy firms have used apps to help customers with their tax calculations and other routine financial tasks. Developing a valuable app also helps to boost the image of the business as one that embraces technology.

ICAEW's Financial Reporting Faculty has a very successful app. Next to be developed is an app that will give student members mobile access to exams results.

For more information on the IT Faculty, visit icaew.com/itfac

AUDIT AND BEYOND

RELATIONSHIPS MATTER

Many of the clarified auditing standards introduced a few years ago had little impact on the way auditors in the UK approach their job. One exception was the revised ISA 550 Related Parties.

The Auditing and Assurance Faculty's latest external audit lecture explored this standard in greater detail and addressed the practical issues for charities and owner-managed businesses.

The clarified standard improved the audit of related parties by introducing a more risk-based approach.

The revised ISA 550 indicates that auditors have the responsibility to identify, assess and respond to the risk of material misstatement; it also recognises that fraud can be more easily committed through related parties.

The ICAEW has published a guide, *The Audit of Related Parties in Practice*, to help auditors be more effective in this line of work. It sets out a five-point action plan.

Auditors must first ensure they plan thoroughly. next, look out for material misstatement. Make sure you understand all the relevant internal controls, and design procedures to respond to the risks identified.

Finally, perform completion procedures, including obtaining management representations.

For more information on the Audit and Assurance Faculty, visit icaew.com/aaf

And finally...

"Good grief! This balance-sheet won't do—why damn it, a child could understand it."

HAVING IT ALL

Leadership, communication and customer service. They are all vital skills for those who want to make it as an accountant - in business or in practice. It's no longer enough to be a proficient number-cruncher if you want to get ahead in the profession - you need skills stretching beyond a traditional mastering of numbers.

The days when accountants played a narrow finance role in the organisation are long gone. Finance people today have a much broader role across all departments – they get involved in strategy and key decision-making so it is crucial that they can see the bigger picture.

A survey by Accountemps, the temporary recruiting firm for finance and accounting, reinforces the view that to be an attractive candidate you really do need to have it all.

As the rest of the organisation has become more reliant on the finance function, it is also of more importance for accountants to gain non-accounting skills. When more than 2,100 CFOs were asked what skills they rated most highly in addition to traditional accounting skills, a third placed general business knowledge top of the list. A quarter valued IT skills highly, while communication skills were highly rated by 14%. Leadership and customer service abilities each scored 13%.

Finance people today have a much broader role across departments

Accountants should be able to build great relationships with clients and colleagues through excellent communication skills and a good sense of customer service, while also understanding general business issues – this will help in understanding the needs of the clients as well as what's going on in their own organisation. Being able to explain and understand a company's accounts is no longer enough; you also need to understand how new developments affect the company and the industry in which it operates

THE LAWSON INQUIRY

The Parliamentary Commission on Banking Standards features a starring role for former chancellor Nigel Lawson

BAA: What do you think Mark Carney brings to the role of Bank of England governor?
NL: Sometimes it's good just to be seduced by the particular cheeses spread out in front of you on a cheese counter.

BAA: I see. Turning to reporting standards, what's your take on the proposed amendments to IAS 39?
NL: This is a cross between Pears Belle Helene and Eve's Pudding, but the only important thing to remember is that this is easy, quick, very comforting and seems to please absolutely everyone.

BAA: Well, perhaps not everyone. But, ahem, the proof of the pudding is in the eating. Do you think national regulators will have any issues with it?
NL: You'd be surprised how hard it can be to work out what a certain dish is made of when all you get is one spoonful to taste.

BAA: How do you rate the new UK GAAP?
NL: The wonderful thing about this is not just that it tastes gorgeous, but that I get such a sense of calm, blissful satisfaction from cooking without shopping and from salvaging stuff from having to be thrown away.

BAA: The commission has been hard work. You've been cooking up some pretty severe criticisms of reporting and management approaches. Has it taken its toll?
NL: I have to say that cooking from dawn till dusk, stooping over the stove or marching back and forth from kitchen to studio area is taking its toll.

Editor: Excuse me, I thought this was meant to be an interview with Lord Lawson? It's his daughter Nigella you've got here!

BAA: Eek! Yes, thank you Nigella for your, er, excellent tips and insight.

(With apologies to Lord Lawson and Nigella Lawson)

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