

Financial Reporting Brief.



A major highlight of the third quarter of 2014 is the publication of IFRS 9 *Financial Instruments*. There have also been significant updates to the Corporate Governance Code and the new Irish GAAP standards have been amended.

The International Accounting Standards Board (IASB) has published IFRS 9 *Financial Instruments*, effective for accounting periods beginning on or after 1 January 2018. The IASB has also finalised two amendments in relation to its standards on joint ventures/associates, together with proposed amendments on deferred tax. Accounting for leases is also under active review.

The European Financial Reporting Advisory Group (EFRAG) has been actively engaged in publishing a number of research and discussion papers in key financial reporting areas.

The International Integrated Reporting Council (IIRC) has published two papers which address the issues of assurance in relation to integrated reporting. Non-GAAP financial measures continue to be a focus of attention.

The Financial Reporting Council (FRC) has made significant updates to the UK Corporate Governance Code, which include introducing a 'viability statement' on longer-term solvency and liquidity.

The FRC has amended FRS 101 and FRS 102 in a number of respects, with the amended standards

effective for accounting periods beginning on or after 1 January 2015. Other amendments to FRS 102 have also been proposed in relation to pensions. The FRC has also published a consultation document in respect of small and micro entities.

Charities regulators in the UK have published two new Statements of Recommended Practice (SORPs) in line with the planned introduction of FRS 102 in 2015.

The FRC's Financial Reporting Lab (the Lab) has published two new reports commenting on ways in which the quality and transparency of financial reporting may be enhanced.

The supervisory authorities have been active, with the Irish Auditing and Accounting Supervisory Authority (IAASA) publishing its 2013 Annual Report while, at the overall European level, the European Securities and Markets Authority (ESMA) published its final guidelines on enforcement.

This Brief comments on accounting and regulatory developments during the third quarter of 2014.

International Accounting and Related Developments

Financial Instruments – IFRS 9

The IASB has published the final version of IFRS 9 bringing together the classification and measurement, impairment and hedge accounting phases of the IASBs project to replace IAS 39. The final standard is inclusive of a new expected loss impairment model. The standard is effective for accounting periods commencing on or after 1 January 2018.

An Impairment Transition Resource Group (ITRG) has been formed, with the IASB as a member, to support stakeholders on implementation issues that may arise as a result of the new impairment model under IFRS 9.

Equity Method

The IASB has published "Equity Method in Separate Financial Statements", which reinstates the equity method as an accounting option for investments in subsidiaries, associates and joint ventures in an entity's separate financial statements. The amendments to IAS 27 are effective for annual periods beginning on or after 1 January 2016 with earlier application permitted.

Sale or Contribution of Assets.

The IASB has published 'Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)'. The amendments address a conflict between the standards to clarify that the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business. The amendments are effective for annual periods beginning on or after 1 January 2016, with earlier application permitted.

Annual Improvements

The IASB has issued 'Annual Improvements to IFRS 2012 – 2014 Cycle', with the amendments effective for annual periods beginning on or after 1 January 2016. Amendments are being made to four separate standards.

Deferred Tax

An Exposure Draft (ED) of proposed amendments to IAS 12 Income Taxes has been published by the IASB. The purpose is to clarify accounting for deferred tax assets for unrealised losses on debt instruments. Comments are requested by 18 December 2014.

Measurement – Unit of Account

The IASB has published an ED of proposed amendments to the standards on investments in subsidiaries, joint ventures and associates together with those on fair value and impairment. The proposed amendments would clarify that the unit of account is the investment as a whole, with an illustrative example added to IFRS 13.

Rate Regulation

The IASB has published a Discussion Paper (DP) relevant to companies whose business is influenced by a rate regulation regime of some kind, and to consider under which circumstances financial effects arising from rate regulation should be accommodated in financial reporting.

Leases

The IFRS Foundation Staff have published a document setting out the key tentative decisions reached on the leases project during the first half of 2014, together with the reasons for reaching those tentative decisions and the remaining work to be done in completing the project.

The main change to the Exposure Draft published in May 2013 is that the IASB has tentatively decided to propose a single lessor model for the income statement that would require the recognition of interest and amortisation for all leases recognised on a lessee's balance sheet. The FASB has tentatively decided to propose a dual model similar to that proposed in the 2013 ED.

EFRAG Discussion papers

EFRAG has published four papers with the objective of contributing to the development by the IASB of the revised Conceptual Framework and other developments, which are:

- » **Classification of Claims** – the Paper discusses the distinction between debt and equity and also characteristics of how claims on equity should be accounted for
- » **The Business Model** – the Paper concludes that the business model should continue to play a role in financial reporting with financial reporting faithfully representing the business model, with appropriate guidance for a consistent approach to the business model in standard-setting
- » **Separate Financial Statements** - the Paper aims to address practical concerns regarding application of IFRS to separate financial statements including a) clarification of the objective, b) developments on how to account for transaction costs and contingent consideration, c) addressing issues relating to common control transactions, and d) disclosures on distributions to equity holders.
- » **Goodwill** – a Paper "Should Goodwill still not be amortised?" argues that the reintroduction of amortisation of goodwill would be appropriate, and explores possible approaches to remedy shortcomings identified by constituents

Impact of IFRS in E.U.

The EC has launched a public consultation on the Impact of IFRS in the EU. Responses are requested by 31 October 2014. The EC is currently evaluating whether the initial objectives of the IAS Regulation are still relevant and to identify areas for improvement in the functioning of the IAS Regulation.

Integrated Reporting

The International Integration Reporting Council (IIRC) has published two assurance papers which provide an overview of assurance and its relationship to IR. The first paper provides a high-level overview of the benefits of assurance and addresses practical and technical challenges. The second paper provides a detailed look at the issues when applying assurance to integrated reporting including considerations regarding narrative information, future-oriented information, connectivity and using work of others.

Non-GAAP Financial Measures.

The International Federation of Accountants (IFAC) has published its 'International Good Practice Guidance, Developing and Reporting Supplementary Financial Measures'. The Guidance provides recommendations for the use of such measures and builds on the qualitative characteristics of useful financial reporting which should be relevant, complete, neutral, transparent, understandable and verifiable, comparable and timely.

The disclosure of non-GAAP information is currently widely discussed and the International Organisation of Securities Commissions (IOSCO) has issued proposed guidance setting out IOSCO's expectations for issuers for the presentation of non-GAAP financial measures. These include that sufficient information should accompany the measures to aid in their understanding, with transparent presentation and disclosure of calculations.

Valuation of Derivatives

The International Valuation Standards Council (IVSC) has issued a revised exposure draft proposing guidance on the valuation of equity derivatives, it places more emphasis on practical considerations, including consideration of derivative strategies, and additional guidance on the applicability of models and resolution methods.

Financial Reporting Council and related bodies – developments

Corporate Governance

The FRC has published an updated version of the UK Corporate Governance Code. The focus is on the long term health and strategy of listed companies, and raises the bar for risk management. The FRC has confirmed proposals for boards to include a 'viability statement' to provide an improved and broader assessment of long-term solvency and liquidity which it is expected will look forward significantly longer than 12 months. Listed companies will now need to ensure that executive remuneration is designed to promote the longer-term success of the company and demonstrate to shareholders how this is being achieved.

The key changes to the Code include those in relation to:-

- » Going concern, risk management and internal control
- » Remuneration
- » Shareholder engagement

The FRC has also highlighted the importance of the board's role in establishing the 'tone from the top' of the company in terms of its culture and values.

The updated Code has been published with three related documents:-

- » Guidance on risk management and internal control and related financial and business reporting (the Risk Guidance)
- » Guidance for directors of banks on solvency and liquidity risk management and the going concern basis of accounting.
- » Revised auditing standards – ISAs 260, 570 and 700

The revised Code will apply to accounting periods beginning on or after 1 October 2014

Amendments to FRS 101 and FRS 102

The FRC has issued amendments to the new Irish/UK GAAP Standards, as follows:-

- » Updating the requirements on hedge accounting, making hedge accounting more readily available to entities where it is consistent with their risk management processes, consistent with the hedge accounting requirements included in IFRS 9
- » Relaxing the conditions for regarding financial instruments as 'basic', with the effect that more financial instruments will be measured at cost rather than fair value
- » FRS 101 – the amendments made are to align with changes to IFRS and include those on a) the exemptions from IFRS 10 and IFRS 12 in respect of investment entities, and b) impairment-recoverable amount disclosures

The amendments are effective from 1 January 2015, consistent with FRS 101 and FRS 102.

Proposed Amendments to FRS 102

The FRS has issued an Exposure Draft (ED) with proposed amendments to clarify issues relating to accounting for defined benefit pension plans, including:-

- » No additional liabilities need be recognised in respect of a 'schedule of contributions' that has been agreed in order to address a deficit in the plan
- » The effect of restricting the recognition of a surplus in a defined benefit plan, where the surplus is not recoverable is recognised in other comprehensive income, rather than profit or loss

Small Entities

The FRC has issued a consultation document *Accounting Standards for Small Entities – Implementation of the EU Accounting Directive*. This follows changes in EU law which provide for small companies to include less information in their accounts and fewer mandatory disclosures. The FRC proposes to issue a new accounting standard for micro-entities. The FRC will also introduce a new section into FRS 102 so that the underlying accounting by small entities will in future be consistent with the standard used by other entities – however, the presentation and disclosure requirements for small entities may be more straightforward.

The FRC proposes to withdraw the existing Financial Reporting Standard for Smaller Entities (FRSSE).

Charities SORP

Two new SORPS on accounting by charities has been published which are effective for accounting periods beginning on or after 1 July 2015. The SORPs provide a comprehensive framework for charity accounting and the new SORPs were needed due to the planned introduction of FRS 102 in 2015. The SORPs are mandatory for UK charities and are considered best practice for Irish charities.

Financial Reporting Lab

The Lab has published two insight reports, as follows:-

- » **Towards Clear and Concise Reporting** – the report examines progress made by companies towards producing relevant and succinct annual reports and accounts, and provides ideas on how companies can make further progress in such areas as a) communication channels and how to match information to users' needs, b) how to focus content on what is important to investors, and c) eliminating immaterial disclosures, and
- » **Accounting Policies and Integration of Financial Information** - the report provides valuable insight for companies, based on a survey of a wide range of interested parties, of what investors want from accounting policy disclosures and where they should appear in the financial statements. Matters specifically referred to include a) the avoidance of boilerplate text by being specific to the company and providing sufficient detail to understand the specifics of how the company accounts for its transactions, and b) the need to gain a better understanding of the impact of judgement and estimation on reporting of a company's results and financial position.



Legal and Regulatory Developments

IAASA

IAASA's eight Annual Report has been published. The Report provides a detailed analysis of IAASA's activities during 2013 in its principle functional areas. Chapter 3 of the Report sets out the key activities undertaken in 2013 by IAASA in relation to its financial reporting enforcement function. In 2013 IAASA undertook 28 examinations of annual financial reports, together with examinations of interim reports and a number of thematic examinations and reviews in areas considered relevant by ESMA.

ESMA Guidelines

ESMA has published its final Guidelines on the enforcement of financial information published by listed entities in the European Union. The aim is to strengthen and promote greater supervisory convergence in existing enforcement practices amongst EU accounting enforcers.

ESMA and the IFRS Foundation have announced that the two organisations will deepen their co-operation in the consistent application of IFRSs and has published a statement of protocols.

ESG Directive

The European Council has adopted the Directive on disclosure of non-financial and diversity information by large companies and groups, those with more than 500 employees, addressing environmental, social and governance issues. The timeframe for adoption by EU member states means that the groups and companies concerned will be reporting under the new Directive as of their financial year 2017.

Fund Managers

The Central Bank has published a consultation document entitled 'Fund management companies' effectiveness – delegate oversight'. The consultation focuses on four key measurers:-

- » Draft guidance on good practices for the oversight of the activities of delegates.
- » Streamlining of the number of designated managerial functions
- » Adjusting the requirements for Irish resident directors
- » A new requirement to document the rationale for the composition of the board.

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