Quarterly Financial Reporting Brief

April 2017

The first quarter of 2017 has seen considerable focus on corporate governance, and developments in relation to the Irish/ UK accounting standards with financial instruments and integrated reporting amongst the other areas under consideration.

Brexit has also taken on new life with the triggering of Article 50 leading to a period of evolution which will continue for some time. In addition to the economic and business consequences, there will also be many questions to be answered with regard to such matters as the financial reporting framework and the IFRS adoption process in the UK.

The UK Financial Reporting Council (FRC) has been active in relation to corporate governance and stewardship, publishing its annual report together with announcing plans for a fundamental review of the UK Corporate Governance Code. The FRC has also responded to the UK Government's Green Paper on corporate governance reforms.

The FRC is proposing a number of amendments to FRS 102 following its triennial review. It has also issued a revised edition of FRS 103 which incorporates the amendments arising from Solvency II. The Financial Reporting Lab has issued its report on supplier relationships and a short questionnaire seeking views on future direction, together with launching a consultation process on viability reporting.

The International Accounting Standards Board (IASB) has added a limited scope proposal to its agenda on IFRS 9, and has published an exposure draft of annual improvements 2015/ 2017. The complex area of macro-hedge accounting is also under consideration.

An Exposure Draft has been published proposing changes on segment reporting.

The International Integrated Reporting Council (IIRC) is consulting on the implementation of the IR Framework to inform further development. The International Federation of Accountants (IFAC) has published a position paper supporting integrated reporting.

The Irish Accounting and Auditing Supervisory Authority (IAASA) has adopted the Auditing Framework for Ireland (the standards). IAASA has also published a snapshot of its financial reporting supervisory activities during 2016.

This Brief comments on financial reporting and legal/regulatory developments during the first quarter of 2017.

Ireland and UK – New Developments

Corporate Governance and Stewardship

There have been a number of significant developments in this area, which include the following:

FRC Annual Report

The FRC has published a report 'Developments in Corporate Governance and Stewardship 2016' . The FRC expresses concern at what it sees as a backdrop of falling public trust in business. It has taken steps to improve confidence in the ways companies are governed, including the disclosure of long-term viability statements, improved risk reporting and greater focus on boardroom diversity. Compliance with the principles of the UK Corporate Governance Code remains high, but when boards choose not to follow provisions, the quality of explanations needs to improve and there needs to be more focused reporting by boards on how they discharge their responsibilities. Boards need to be better informed on the link to strategy and business value and need to address succession planning and diversity.

Review of UK Code

The FRC has announced plans for a fundamental review of the UK Corporate Governance Code. This will take account of work it has already done on corporate culture and succession planning in addition to issues raised by the Government in its enquiries. The FRC will commence a consultation later in 2017 to seek input from a wide range of stake holders including its recently established Stakeholder Advisory Panel, comprised of high profile representatives from a wide range of sectors.

Corporate Governance Reforms

The FRC has responded to the Government's Green Paper on corporate governance reforms. The interests of stakeholders, executive remuneration, the accountability of large private companies and effective enforcement are key themes in the FRC'S response. The FRC emphasises that companies should be required to report more effectively on how they promote success having regard to a range of factors such as long-term consequences, the environment, employees, suppliers and customers.

FRS 102 – Triennial Review

Arising from its triennial review of FRS 102 and taking account of stakeholder feedback on the implementation of the standard, the FRC is proposing a number of amendments. The principal amendments proposed are simplifications designed to make it more cost effective to apply and easier to use FRS 102 and they include:

- Simplifying the accounting for directors loans by small entities by no longer requiring a market rate of interest to be estimated
- Requiring fewer intangible assets to be separated from goodwill in a business combination
- Permitting investment property rented to another group entity to be measured based on cost (rather than fair value).

In addition, amendments proposed to the classification of financial instruments will allow more of them to be measured based on cost and fewer entities will be classified as financial institutions which are required to provide enhanced disclosures about financial instruments.

The FRC aims to finalise the amendments in December 2017 with an effective date of accounting periods beginning on or after 1 January 2019. Early application will be permitted.

Insurance Contracts

The FRC has issued a revised edition of FRS 103: Insurance Contracts. The revised edition incorporates the amendments arising as a result of Solvency II that was issued in May 2016.

The amendments to FRS 103 principally update a number of definitions. They do not require insurers to change their accounting policies. However, some insurers may wish to do so to make them more consistent with Solvency II, and these amendments clarify that.

Financial Reporting Lab

The Financial Reporting Lab has published a report on disclosures of supplier relationships and commercial income, working with one particular supermarket chain as a basis for their comments and recommendations. The report notes that investors wish to understand the quality of supplier relationships and their place in a retailer's wider business model. Enhanced disclosures provided by the supermarket group were in the accounting policies note, the CFO report and financial review and the audit committee report. The report drew out different aspects of its relationships with its supply base as part of its business model disclosures.

The Lab has also invited companies, investors and analysts to participate in a project on effective risk and viability reporting. This project follows the publication of the Lab report on Business Model reporting which was published in October 2016. It will explore how companies can develop effective principal risk reporting and viability statement reporting to meet the needs of investors.

The Lab has issued a short questionnaire to obtain constituent views on the future direction of the Lab and the work to be undertaken.

Climate-Related Disclosures

The FRC has responded to the Financial Stability Board's task force consultation, supporting the proposals as stimulus to develop thinking in the area but urging caution to a list of suggested disclosures which may risk companies adopting a checklist mentality and boilerplate approach.

The Sustainability Accounting Standards Board has also responded to the consultation, making several additional recommendations calling for more guidance to be included and clarity on materiality.

International Accounting and Related Developments

Financial Instruments

The IASB has added a limited scope project on IFRS 9 to its agenda, to look into whether a narrow-scope exception could be made to allow investments with symmetric prepayment options to qualify for amortised cost or fair value measurement through other comprehensive income.

EFRAG has conducted targeted outreach among 15 banks regarding whether current hedge accounting requirements, under IFRS 9, accommodate the way a bank manages interest rate risk. The feedback adds further confirmation that a new high quality macro-hedge accounting solution is needed to deal with reporting the effect of dynamic risk management activities in financial statements.

The Basel Committee on Banking Supervision (BCBS) has released a statement on the interim regulatory treatment of accounting provisions and standards. BCBS stresses that it supports the use of the expected credit loss accounting approach to impairment provisions but, in view of the limited time until the effective date of IFRS 9, it has decided to retain the current regulatory treatment of provisions for an interim period and will thoroughly review the longer-term regulatory treatment.

Annual Improvements

The IASB has published an exposure draft of Annual Improvements for its 2015/ 17 cycle, with proposed amendments to three standards, and comments are requested by 12 April. The standards for proposed amendment, and the subject areas, are:

- IAS 12 : Income Taxes – income tax consequences of dividends
- IAS 23 : Borrowing Costs – treatment of borrowings on completion of project
- IAS 28 : Investments in Associates and Joint Ventures – IFRS 9 treatment of long-term interests in net investment.

Operating Segments

The IASB has published an exposure draft 'Improvements to IFRS 8 : Operating Segments', containing proposed amendments in five areas:

- Description of the chief operating decision maker – improve clarity of function
- Identification of reportable segments – disclosure of reasons if segments are different
- Additional segment information – to clarify that additional information may be provided
- Description of reconciling items – sufficient explanations to be provided of reconciling items
- Change in composition of an entity's reportable segments – to clarify interim reporting requirements.

An effective date is not proposed, but it is indicated that earlier application would be permitted. Comments are requested by 31 July 2017.

Disclosure Principles

The IASB has published a comprehensive discussion paper setting out its preliminary view on disclosure principles that should be included in a general disclosure standard or in non-mandatory guidance on the topic. This is one of the key components in the IASB's 'Better Communication' central theme for development in the period 2017 to 2021, which also includes the primary financial statements project and the IFRS Taxonomy with a related project being the Conceptual Framework. Guidance on materiality is also in the pipeline. The DP includes an executive summary describing the reasons behind publishing the DP, the preliminary views of the IASB and the next steps. Comments are due on or before 2 October 2017.

ESMA Decisions

ESMA has published a twentieth extract from its confidential database of enforcement decisions taken by European national enforcers. The batch deals with 13 standards and one interpretation. The purpose of the publication of these decisions is to assist entities with consistent application and serve as a reference point for interpretation.

Integrated Reporting

IFAC has published its Policy Position Paper 8 on enhanced organisational reporting which emphasises its view that integrated reporting is the way to achieve a more coherent corporate reporting system. IFAC sees the integrated report as enabling greater interconnectedness between different reports, recognising that there is a range of different frameworks and regulations available, and under development.

Three years after publication of the IR Framework, the IIRC has announced a two month consultation period with feedback sought from preparers of reports, providers of financial capital and other users of integrated reports as well as policy makers, standard setters and regulators. The purpose is to gauge businesses' views on the implementation of the framework, to inform further development.

On a similar note:

- The London Stock Exchange has issued guidance setting out its recommendations for good practice in Environmental, Social and Governance reporting (ESG).
- The Global Reporting Initiative (GRI) has published a linkage document showing how the GRI Standards can be used to comply with all aspects of the European Directive on the disclosure of non-financial and diversity information.

Alternative Performance Measures

The CFA Institute, a global association of investment professionals, has published two reports dealing with the investor perspective on non-GAAP financial measures. The first paper acknowledges that they are useful for investors but there are concerns around consistency, comparability across periods and similar companies, and transparency of non-GAAP financial measures. The second paper articulates actions to improve communication and enhance performance reporting with calls to securities regulators to improve discipline around reporting of non-GAAP measures, and to the IASB/FASB to enhance primary financial statements presentation and classification which could reduce the perceived need for such measures.

Public Sector Combinations

The International Public Sector Accounting Standards Board (IPSASB) has released IPSAS 40 : Public Sector Combinations. IPSAS 40 classifies public sector combinations as either amalgamations or acquisitions taking into account control and other factors. Amalgamations are to be accounted for using the 'modified pooling interests' method of accounting, with acquisitions accounted for using the same approach as IFRS 3.

The Standard applies from 1 January 2019 with earlier adoption encouraged.

Valuation Standards

The International Valuation Standards Council (IVSC) has issued its 2017 suite of standards. IVS 2017 consists of five general standards and six asset standards, related to specific types of assets. The general standards offer guidance for engagement terms, basis of value, valuation approaches and methods and reporting.

XBRL

The IFRS Foundation has published its 2017 IFRS Taxonomy which is consistent with IFRS as issued by the IASB at 1 January 2017.

Legal and Regulatory Developments

IAASA Developments

IAASA has adopted the Auditing Framework for Ireland (The Standards) following on from the EU Audit Regulations signed into Irish law in June 2016 which made IAASA responsible for adoption of Standards in Ireland. The standards are available here.

Feedback received by IAASA in response to its consultation on the future framework continues to be reviewed.

IAASA also published a snapshot of its financial reporting activities during 2016, with reports of 45 entities examined and 61 undertakings made by 19 companies regarding remedial measures to be taken with their reports.

Companies (Accounting) Bill 2016

The Accounting Bill continues through the legislative process, with the most recent development of note being a proposal to amend the Bill regarding the proposed introduction of an obligation for private unlimited companies to file their accounts. The effect of the amendment will be to defer the application of this provision, which will only come into operation on 1 January 2022 for any financial year which commences after that date.

Code of Practice – State Bodies

The Code of Practice for the Governance of State Bodies (2016) is effective for financial reporting periods beginning on or after 1 September 2016. A clarification note has been issued to that effect. For periods before that date, State Bodies have the option to use the 2009 Code or elect to apply the 2016 Code early.

Supervisory Authorities – EU Consultation

The European Commission has launched a public consultation on the operation of the European Supervisory Authorities (ESAs) one of which is the European Securities and Markets Authority (ESMA). The consultation suggests that the review of the ESAs' operation might also be used to "streamline" the endorsement process in the EU by giving ESMA an "advisory role".

Deloitte.

Contact Us

Our firm's website, www.iasplus.com, provides a world-leading continuously updated information source on international financial reporting developments and includes a link to our freely accessible IFRS eLearning programme, and a focused subsite, UK Accounting Plus.

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