The UK Accounting Standards Endorsement Board

OPINION

Introduction

1. Pursuant to regulation 7(1)(a) of The International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (the "**2019 Regulations**"), the Secretary of State is tasked with the responsibility of determining whether an international accounting standard,[1] which it is proposed be adopted for use in the United Kingdom, is 'not contrary' to either of the following principles:

   (1) an undertaking's accounts must give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss;

   (2) consolidated accounts must give a true and fair view of the assets, liabilities, financial position and profit or loss of the undertakings included in the accounts taken as a whole, so far as concerns members of the undertaking.

2. The Secretary of State has delegated this responsibility to the UK Accounting Standards Endorsement Board, an unincorporated association established on 26th March 2021 (the "**UK Endorsement Board**"). We are instructed by the UK Endorsement Board to advise on a number of issues pertinent to its performance of that responsibility. Those issues are as follows:

   (1) the relationship between *(i)* the 'true and fair' principle as referred to in regulation 7(1)(a) of the 2019 Regulations and *(ii)* the duty of directors of a company under section 393(1) of the Companies Act 2006 (the "**CA 2006**");

   (2) the entities to which international accounting standards adopted for use in the UK under the 2019 Regulations apply;

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[1] The 2019 Regulations adopt the definition of 'international accounting standards' contained in Article 2 of Regulation (EC) No. 1606/2002, which is quoted in paragraph 8 of the Opinion below. We adopt the same definition for the purposes of this Opinion; and references to 'international accounting standards' and 'standards' should be read accordingly.

(3) whether the following view, expressed by Martin Moore Q.C. in an opinion written for the Financial Reporting Council in 2008, remains appropriate under the law of England and Wales[2]:

> "the true and fair view, or fair presentation, concept is of an overarching nature. Any decision made or judgment reached by the preparer of financial statements is not made in a vacuum but is made against the requirement to give a true and fair view, or to achieve a fair presentation".

(4) whether, in reaching its view under regulation 7(1)(a), the UK Endorsement Board can assume that, if the specific standard is adopted, the directors of a company preparing financial statements using the UK-adopted international accounting standards will retain the ability to reflect a true and fair view in those financial statements.

(5) whether, in determining whether an international accounting standard is 'not contrary' to the true and fair principle as referred to regulation 7(1)(a) of the 2019 Regulations, the UK Endorsement Board is required to assess that standard in isolation or together with the other previously UK-adopted international accounting standards;

(6) whether there is any requirement under English law following the UK's departure from the EU that the true and fair test should be applied individually to assets, liabilities, financial position, profit or loss items in the financial statements, or whether the test should be applied to the collective effect of those items.

3. Our views, in summary, are as follows:

(1) The references to the true and fair principle in the 2019 Regulations and in section 393 of the CA 2006 are to the same concept, the meaning of which has been the subject of a number of legal opinions that have received judicial endorsement (to which reference is made below). However, the duty of the UK Endorsement Board under the regulation 7(1)(a) of the 2019 Regulations is different from the duty of directors under section 393(1) of the CA 2006. The duty of the Board under regulation 7(1)(a) is to determine generically, before the standard is applied to a set of accounts, whether a proposed international

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2 Our instructions seek advice on the position under the law of the United Kingdom. However, our expertise is the law of England and Wales, and accordingly this Opinion is prepared by reference to the position under that legal system.

accounting standard is 'not contrary' to the true and fair principle. By contrast, the duty of directors under section 393(1) is to be satisfied that a particular set of accounts give a true and fair view.

(2) International accounting standards adopted for use under the 2019 Regulations will apply not simply to entities obliged to prepare their accounts in accordance with those standards under section 403(1) of the CA 2006, but also to those entities who elect to do so under section 395(1) or section 403(2) of the CA 2006.

(3) We consider that the view expressed by Mr. Moore, quoted above, does remain appropriate under the law of England and Wales.

(4) On the current formulation of IAS1 as adopted for use in the UK, directors retain the ability to reflect a true and fair view of the assets, liabilities, financial position and profit or loss of the company in its financial statements, even where this would involve a departure from the relevant accounting standards; indeed, their duty under section 393(1) of the CA 2006 requires them to be satisfied that the accounts do give a true and fair view. However, the existence of a true and fair override does not enable the UK Endorsement Board to outsource the decision as to whether a proposed accounting standard is not contrary to the true and fair principle to directors. The UK Endorsement Board is subject to a duty under regulation 7(1)(a) to reach its own view that the proposed standard is not contrary to the true and fair principle.

(5) The UK Endorsement Board must reach the view that a standard will not be contrary to the true and fair view principle on both a stand-alone basis and in conjunction with other UK-adopted international accounting standards.

(6) For the purposes of fulfilling its regulatory responsibility under regulation 7(1)(a) of the 2019 Regulations, the UK Endorsement Board must reach the view that a proposed standard does not prevent accounts from giving a true and fair view in respect of any of the specific items identified in regulation 7(1)(a) (namely, the undertaking's assets, liabilities, financial position and profit or loss) when considered in the context of the preparation of the accounts as a whole.

Analysis

4. Before addressing the specific issues on which we are asked to advise, we summarise the background to the 2019 Regulations and our understanding of the approach taken to the concept of 'true and fair' under English law.

Background to the 2019 Regulations

5. 'Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19th July 2002 on the application of international accounting standards' (the "**IAS Regulation**") concerns the adoption and use of international accounting standards in the European Union. By article 4 of that regulation, companies governed by the law of a member state of the EU are required to prepare their consolidated accounts in conformity with the international accounting standards which have been adopted by the EU if, at their balance sheet date, their securities are admitted to trading on a regulated market of any member state. Member states may also permit or require non-publicly traded companies to prepare their consolidated and/or annual accounts in conformity with those standards.

6. The process for the adoption of international accounting standards in the EU is set out in article 3 of the IAS Regulation. Article 3(2) provides:

> "The international accounting standards can only be adopted if:
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> - they are not contrary to the principle set out in Article 2(3) of Directive 78/660/EEC and in Article 16(3) of Directive 83/349/EEC and are conducive to the European public good, and
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> - they meet the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management."

7. The principle set out in Article 2(3) of Directive 78/660/EEC was that, in summary, the annual accounts of companies limited by shares and by guarantee (whether public or private) "*shall give a true and fair view of the company's assets, liabilities, financial position and profit or loss*". Article 16(3) of Directive of 83/349 EEC referred to the same principle in the context of the preparation of consolidated accounts. The application of that principle to the preparation of individual and consolidated accounts was reconfirmed by the Accounting Directive (2013/34/EU), which replaced Directives

78/660/EC and 83/349/EEC (see recital 42 and articles 4(3) and 24 of the Accounting Directive).

8. The IAS Regulation defines 'international accounting standards' as "*International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and related Interpretations (SIC-IFRIC interpretations), subsequent amendments to those standards and related interpretations, future standards and related interpretations issued or adopted by the International Accounting Standards Board (IASB)*". The standards which have been adopted for use in the EU are contained in Commission Regulation (EC) No. 1126/2008 of 3rd November 2008 adopting certain international accounting standards in accordance with Regulation (EC) No. 1606/2002 of the European Parliament and of the Council.

9. The effects of the IAS Regulation were transposed into UK law by Part 15 of the CA 2006 and regulations made under that Part. As a result, prior to the UK's departure from the EU, under the CA 2006, publicly traded companies in the UK were required to apply the international accounting standards as endorsed and adopted by the EU to their consolidated accounts, whilst (with one exception[3]) all other companies were required to produce their accounts either (i) using the international accounting standards or (ii) in accordance with section 396 (in the case of individual accounts) or section 404 (in the case of group accounts) of the CA 2006.

10. Following the UK's departure from the EU, the EU's acquis[4] was frozen in time and directly applicable EU law became UK legislation, by virtue of the European Union (Withdrawal) Act 2018. This meant that international accounting standards, as endorsed by the EU, were brought into UK law but frozen as at the date of the end of the implementation period following the UK's departure from the EU; future adoptions, interpretations and amendments of the IFRS as adopted by the EU no longer apply in the UK.[5]

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3 The exception is in respect of a company that is a charity, whose individual and (where appropriate) group accounts must be prepared in accordance with, respectively, sections 396 and 404 of the CA 2006: see sections 395(2) and 403(3).

4 The EU's 'acquis' is the body of common rights and obligations that are binding on all EU member states.

5 See also regulation 4 of the 2019 Regulations (as amended by regulation 23(b) of The Companies and Statutory Auditors etc. (Consequential Amendments) (EU Exit) Regulations 2020) which provides: "*The international accounting standards adopted for use within the United Kingdom on IP completion day are those which were contained in Commission Regulation (EC) No. 1126/2008 of 3 November 2008 adopting*

11. As identified in the Explanatory Memorandum to the 2019 Regulations, the UK Government considered it to be in the UK's interest to maintain convergence with IFRS following its departure from the EU. As a result, the UK required a national framework to adopt new standards and/or changes to existing standards, by way of substitution for the mechanism which applies in the EU. To that end, the Secretary of State has made the 2019 Regulations.

12. The 2019 Regulations entrust responsibility for the adoption of international accounting standards to the Secretary of State (but with a power to delegate its functions) and set out the basis on which they might be adopted. Of relevance for present purposes is regulation 7(1), which states:

> "The Secretary of State may only adopt an international accounting standard under regulation 6 if the Secretary of State is of the view that, in relation to the form of the standard the Secretary of State intends to adopt-
>
> (a) the standard is not contrary to either of the following principles-
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> (i) an undertaking's accounts must give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss;
>
> (ii) consolidated accounts must give a true and fair view of the assets, liabilities, financial position and profit or loss of the undertakings included in the accounts taken as a whole, so far as concerns members of the undertaking;
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> (b) the use of the standard is likely to be conducive to the long term public good in the United Kingdom; and
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> (c) the standard meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management."

13. This mirrors, to a significant extent, the criteria by which the European Commission assesses international accounting standards for adoption in the EU under article 3(2) of the IAS Regulation.

14. Regulations 13 and 14 of the 2019 Regulations empower the Secretary of State to delegate its responsibility for assessing and, if appropriate, adopting international accounting standards for use in the UK. In the exercise of that power, it has delegated those functions to the UK Endorsement Board (see The International Accounting

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certain international accounting standards in accordance with Regulation (EC) No. 1606/2002 of the European Parliament and of the Council on the application of international accounting standards, as it had effect immediately before IP completion day". "*IP completion day*" was 31st December 2020 at 11.00 p.m. (section 39(1) of the European Union (Withdrawal Agreement) Act 2020).

Standards (Delegation of Functions) (EU Exit) Regulations 2021 (the "**2021 Regulations**")).

The 'true and fair' concept

15. Section 393(1) of the CA 2006 provides as follows:

> "The directors of a company must not approve accounts for the purposes of this Chapter [Chapter 4 of Part 15] unless they are satisfied that they give a true and fair view of the assets, liabilities, financial position and profit or loss-
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> (a) in the case of the company's individual accounts, of the company;
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> (b) in the case of the company's group accounts, of the undertakings included in the consolidation as a whole, so far as concerns members of the company."

16. This duty applies irrespective of whether the accounts to be approved under Chapter 4 of Part 15 of the CA 2006[6] are prepared in accordance with either: *(i)* the regulations made by the Secretary of State under section 396 (in the case of individual accounts) or section 404 (in the case of group accounts) of the CA 2006 (together, "**Companies Act accounts**"); or *(ii)* UK-adopted international accounting standards ("**IAS accounts**"). In the case of Companies Act accounts, there are further statutory provisions which also refer to the 'true and fair' concept, as follows:

(1) In the case of a company's individual accounts, section 396(2) of the CA 2006 states:

> "The accounts must-
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> (a) in the case of the balance sheet, give a true and fair view of the state of affairs of the company as the end of the financial year, and
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> (b) in the case of the profit and loss account, give a true and fair view of the profit or loss of the company for the financial year."

(2) To like effect, in the case of consolidated accounts, section 404(2) provides:

> "The accounts must give a true and fair view of the state of affairs as at the end of the financial year, and the profit or loss for the financial year, of the undertakings included in the consolidation as a whole, so far as concerns members of the company."

17. The concept of 'true and fair view' was the subject of Joint Opinions written by Leonard Hoffmann Q.C. and Mary Arden (as they then were) dated 13th September 1983 and

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6 Part 15 of the CA 2006 relates to the preparation of financial accounts and reports.

20th March 1984 and a further Opinion written by Mary Arden Q.C. dated 21st April 1993 (collectively, the "**Opinions**"). The Opinions were written by reference to the true and fair requirement as it appeared in the statutory predecessor provisions to sections 396(2) and 404(2) of the CA 2006. In this connection, the true and fair requirement has existed under English law since 1947 (its first appearance was in section 13(1) of the Companies Act 1947). Section 393(1) of the CA 2006 appeared for the first time in the CA 2006 (there being no predecessor provision in earlier Companies Acts). Nevertheless, in his Opinion for the Financial Reporting Council in 2008, Martin Moore Q.C. expressed the view that section 393 would not be taken to have altered the central conclusion set out in the Opinions, on the basis that the reason for its introduction was a desire on the part of the legislature to clarify an existing concept. We agree.

18. The Opinions observed that 'true and fair view' is a legal concept and it is for the courts to decide in any given case whether accounts do give a true and fair view. However, they noted the role to be played by the ordinary practices of professional accountants in the court's determination of this question, as follows:

> "7. It is however important to observe that the application of the concept involves judgment in questions of degree. The information contained in accounts must be accurate and comprehensive (to mention two of the most obvious elements which contribute to a true and fair view) to within acceptable limits. What is acceptable and how is this to be achieved? Reasonable businessmen and accountants may differ over the degree of accuracy or comprehensiveness which in particular cases the accounts should attain. Equally, there may sometimes be room for differences over the method to adopt in order to give a true and fair view, cases in which there may be more than one "true and fair view" of the same financial position. Again, because "true and fair view" involves questions of degree, we think that cost-effectiveness must play a part in deciding the amount of information which is sufficient to make accounts true and fair.
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> 8. In the end, as we have said, the question of whether accounts give a true and fair view in compliance with the Companies Acts must be decided by a judge. But the courts look for guidance on this question to the ordinary practices of professional accountants. This is not merely because accounts are expressed in a language which judges find difficult to understand. This may sometimes be true but it is a minor reason for the importance which the courts attach to evidence of accountancy practice. The important reason is inherent in the nature of the "true and fair" concept. Accounts will not be true and fair unless the information they contain is sufficient in quantity and quality to satisfy the reasonable expectations of the readers to whom they are addressed. On this question, accountants can express an informed professional

> opinion on what, in current circumstances, it is thought that accounts should reasonably contain. But they can do more than that. The readership of accounts will consist of businessmen, investors, bankers and so forth, as well as professional accountants. But the expectations of the readers will have been moulded by the practices of accountants because by [and] large they will expect [to] get what they ordinarily get and that in turn will depend upon the normal practices of accountants.
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> 9. For these reasons, the courts will treat compliance with accepted accounting principles as prima facie evidence that the accounts are true and fair. Equally, deviation from accepted principles will be prima facie evidence that they are not."

19. The approach set out in the Opinions has received judicial endorsement, including by Lord Hoffmann himself (see, e.g., *Revenue and Customs Commissioners v. William Grant & Sons Distillers Ltd.* [2007] 1 W.L.R. 1448, H.L., at [2] *per* Lord Hoffmann and at [38] *per* Lord Hope; see also *Macquarie Internationale Investments Ltd. v. Glencore UK Ltd. (No. 2)* [2010] 1 B.C.L.C. 238 (at [167]-[168] *per* Andrew Smith J. and (on appeal) [2011] 1 B.C.L.C. 561, C.A. at [51]-[52] *per* Jackson L.J.).

20. Consistently with this approach, the 2019 Regulations afford a role to those with an interest in the quality and availability of accounts in the process of determining whether a proposed international accounting standard is, *inter alia*, contrary to the true and fair principle. Thus regulation 8 provides:

> "Before adopting an international accounting standard under regulation 6, the Secretary of State must consult such persons as the Secretary of State considers to be representatives of those with an interest in the quality and availability of accounts, including users and preparers of accounts."

21. The role played by such persons in the process of adopting international accounting standards for use in the UK under the 2019 Regulations both ensures that that process is thorough and serves to confirm the view expressed in the Opinions, that the courts will treat compliance with the UK-adopted international accounting standards as *prima facie* evidence that the accounts are true and fair and deviation from those standards as *prima facie* evidence that they are not.

22. Against that background, we turn to the specific issues on which we are asked to opine.

Issue (1): the relationship between the true and fair principle in the 2019 Regulations and section 393 of the CA 2006

23. The references to the true and fair principle in the 2019 Regulations and in section 393 of the CA 2006 are to the same concept. This is confirmed by paragraph 7.5 of the explanatory memorandum which accompanied the 2021 Regulations, which states:

> "To adopt a standard, the UKEB will need to be satisfied that it adheres to the criteria set out in the principal Regulations. The Board can only decide to adopt a standard if it is satisfied that the standard is conducive to the UK's long-term public good and would not be contrary to the principle that accounts must give a "true & fair" view of an undertaking's assets, liabilities, financial position and profit or loss. The latter requirement provides consistency with the requirements on directors of a company in s.393 of the Companies Act 2006."

24. However, the duty of the UK Endorsement Board under the regulation 7(1)(a) of the 2019 Regulations is different from the duty of directors under section 393(1) of the CA 2006. The duty of the Board under regulation 7(1)(a) is to determine generically, before the standard is applied to a set of accounts, whether a proposed accounting standard is 'not contrary' to the true and fair principle. By contrast, the duty of directors under section 393(1) is to be satisfied that a particular set of accounts give a true and fair view.

25. In relation to the duty of the UK Endorsement Board, the following points merit particular emphasis:

    (1) The task of the UK Endorsement Board is to reach a 'view' as to whether the proposed standard is or is not contrary to the true and fair principle. This will require it to balance competing arguments. In carrying out that exercise, the Board must act rationally and must take all relevant factors or considerations into account and exclude from consideration irrelevant matters. It must also act for a proper purpose and follow the correct procedure, which includes not only the requirement under the 2019 Regulations to consult with such persons as it considers to be representative of those with an interest in the quality and availability of accounts (regulation 8) and to publish its reasons for any decision to adopt or not to adopt a standard (regulation 9) but also any policy which it has set for itself (for example in the Due Process Handbook).

    (2) In deciding to adopt an international accounting standard for use in the UK, the UK Endorsement Board must have reached the view, not that the standard is

unlikely to be contrary to the true and fair principle, but that it is not contrary to the true and fair principle. In this regard, one might contrast the language of regulation 7(1)(a) ("*the standard is not contrary*") with that of regulation 7(1)(b) which imposes a lower threshold ("*the use of the standard is likely to be conducive to the long term public good*" (emphasis added)).

(3) This is important because of the weight which the courts will attach to compliance with international accounting standards as adopted under the 2019 Regulations. As noted above, the courts will treat compliance with the UK-adopted international accounting standards as *prima facie* evidence that the accounts are true and fair and deviation from those standards as *prima facie* evidence that they are not.

(4) However, this does not mean that, in reaching its view under regulation 7(1)(a), the UK Endorsement Board needs to be satisfied that all accounts prepared in accordance with the proposed standard will give a true and fair view. This would be an impossible task, not least because the UK Endorsement Board is considering the question in the abstract. But in any event, it is the duty of directors, not the UK Endorsement Board, to ensure that the accounts of the company for which they are responsible give a true and fair view pursuant to section 393(1) of CA 2006. Indeed, as explained further below, for accounts prepared in accordance with UK-adopted international accounting standards, a director's duty under section 393(1) of the CA 2006 may require a departure from those standards notwithstanding the fact that those standards have been adjudged to meet the criteria set out in regulation 7(1)(a), albeit the circumstances in which such a departure will be justified will be "*extremely rare*" (*per* paragraph 19 of IAS1, quoted below).

(5) Relatedly, in reaching its view under regulation 7(1)(a), the UK Endorsement Board does not need to be satisfied that no circumstances could ever arise in which the application of the proposed standard would result in accounts which did not give a true and fair view. However, the UK Endorsement Board does need to be able to conclude that such circumstances would be "*extremely rare*", given that IAS1 requires a departure from compliance with a requirement in an IFRS only in circumstances that are extremely rare, as described further below.

Issue (2): the entities to which international accounting standards adopted for use in the UK under the 2019 Regulations apply

26. Regulation 5 of the 2019 Regulations states as follows:

> "The Secretary of State is responsible for-
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> (a) the adoption of international accounting standards for use within the United Kingdom, with a view to harmonising the financial information presented by the companies required by section 403(1) of the Companies Act 2006 to prepare their accounts in accordance with UK-adopted international accounting standards, in order to ensure-
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> (i) a high degree of transparency and international comparability of financial statements; and
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> (ii) the efficient allocation of capital, including the smooth functioning of capital markets in the United Kingdom; and
>
> (b) participating in and contributing to the development of a single set of international accounting standards."

27. Section 403(1) of the CA 2006 provides:

> "The group accounts of a parent company whose securities are, on its balance sheet date, admitted to trading on a UK regulated market must be prepared in accordance with UK-adopted international accounting standards [...]".

28. This does not mean that, when exercising its power to adopt accounting standards under the 2019 Regulations, the UK Endorsement Board should or need only have regard to the application of the proposed accounting standard to the group accounts of a parent company falling within the scope of section 403(1).

29. The Board's power under regulation 6 of the 2019 Regulations is not limited to the adoption of international accounting standards for use by companies falling within the scope of section 403(1) in the preparation of their group accounts, but extends to the adoption of international accounting standards for use within the UK generally. Consistently with this, regulation 7(1)(a) provides that the Board may only adopt a standard if it is of the view that the standard is not contrary to the principle that consolidated accounts must give a true and fair view, but also that it is not contrary to the principle that an undertaking's accounts must give a true and fair view. The latter requirement would be redundant if the UK Endorsement Board was only concerned with the adoption of standards for use in the preparation of a listed company's group accounts.

30. This conclusion is unsurprising, because it is not just companies falling within the scope of section 403(1) of the CA 2006 for whom the standards adopted by the UK Endorsement Board may be relevant. Whilst such companies are obliged to prepare their group accounts in accordance with UK-adopted international accounting standards, all other companies (with the exception of charities) may elect to prepare their individual and/or group accounts in accordance with UK-adopted international accounting standards too (see sections 395(1)(b) and 403(2)(b) of the CA 2006).

Issue (3): the role of the 'true and fair' concept in the preparation of accounts

31. As noted above, in his 2008 Opinion for the Financial Reporting Council, Martin Moore Q.C. expressed the view (at paragraph 4(H)) that:

> "the true and fair view, or fair presentation, concept is of an overarching nature. Any decision made or judgment reached by the preparer of financial statements is not made in a vacuum but is made against the requirement to give a true and fair view, or to achieve a fair presentation."

32. We have been asked whether it remains appropriate to say that the true and view concept is of an overarching nature under English law. We consider that it is.

33. Section 393(1) of the CA 2006, to which we referred above, imposes a duty on directors (in summary) not to approve accounts unless they give a true and fair view. The explanatory notes which accompany the CA 2006 explain (at paragraph 646) that this duty amounts to an "*overarching obligation on directors (the preparers of accounts)*". Consistently with this, as noted above, the duty applies irrespective of whether the accounts are Companies Act accounts or IAS accounts.

34. The overarching nature of the concept in the preparation of accounts is consistent with the duties imposed by the CA 2006 on auditors. In carrying out their functions under the CA 2006 in relation to the company's annual accounts, the auditor must have regard to the director's duty under section 393(1) (section 393(2) of the CA 2006), and their report must state clearly whether, in their opinion, the annual accounts, *inter alia*, give a true and fair view: in the case of an individual balance sheet, of the state of affairs of the company as at the end of the financial year; in the case of an individual profit and loss account, of the profit and loss of the company for the financial year; and in the case of group accounts, of the state of affairs as at the end of the financial year and of the profit or loss for the financial year of the undertakings included in the consolidation as a whole, so far as concerns members of the company (section 495(3) of the CA 2006).

35. The overarching nature of the 'true and fair' concept is also reflected in the fact that, in the case of the Companies Act accounts, there is an express statutory override: by reason of section 396(5) (in the case of individual accounts) and section 404(5) (in the case of group accounts), the requirement to achieve a true and fair view when preparing accounts takes precedence over some other specific legislative provision relating to the preparation of Companies Act accounts.

36. Whether there exists an equivalent override in the case of IAS accounts was the subject of debate in a series of Opinions provided by Martin Moore Q.C. to the Financial Reporting Council in 2008 and 2013 (who concluded that there was) and by George Bompas Q.C. in 2013 and 2015 (who expressed doubts on the issue). The debate centred around whether International Accounting Standard 1 ("**IAS1**"), which concerns the presentation of financial statements, contains such an override. IAS1 has been adopted for use in the EU, and (by reason of regulation 4 of the 2019 Regulations) it has been adopted for use in the UK following its exit from the EU too.

37. To the extent that there remains any doubt over the question, we adhere to the view that IAS1 does contain such an override. The material provisions of IAS1 include the following:

(1) Paragraph 15 of IAS1 provides:

> "Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Conceptual Framework for Financial Reporting (Conceptual Framework). The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation."

Mr. Moore expressed the view, with which Mr. Bompas appears not to have disagreed, that 'present fairly' and 'true and fair' are articulations of the same concept.

(2) Paragraph 19 of IAS1 then provides:

> "In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the Conceptual Framework, the entity shall depart from that requirement in the manner set out in

paragraph 20 if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure."

(3) As foreshadowed in paragraph 19, paragraph 20 explains what should be done in the event of a departure from a requirement in an IFRS:

> "When an entity departs from a requirement of an IFRS in accordance with paragraph 19, it shall disclose:
>
> (a) that management has concluded that the financial statements <u>present fairly</u> the entity's financial position, financial performance and cash flows;
>
> (b) that it has complied with applicable IFRSs, except that it has departed from a particular requirement <u>to achieve a fair presentation</u>;
>
> (c) the title of the IFRS from which the entity has departed, the nature of the departure, including the treatment that the IFRS would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the objective of financial statements set out in the Conceptual Framework, and the treatment adopted; and
>
> (d) for each period presented, the financial effect of the departure on each item in the financial statements that would have been reported in complying with the requirement."
>
> (Emphasis added.)

(4) Paragraph 24 explains the circumstances in which information would conflict with the objective of financial statements:

> "For the purpose of paragraphs 19-23, an item of information would conflict with the objective of financial statements when it does not represent faithfully the transactions, other events and conditions that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to influence economic decisions made by users of financial statements. [...]"

(5) Finally, for completeness, the 'Conceptual Framework for Financial Reporting' (March 2018),[7] to which IAS1 refers, states (at paragraph 1.2) that "*[t]he*

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7 The 'Conceptual Framework for Financial Reporting' is issued by the IASB. It is not itself an accounting standard and has not been expressly adopted for use in the UK, although (as noted above) it is referred to in IAS1. The Conceptual Framework describes the objective of, and the concepts for, general purpose financial reporting. Its purpose is to: (a) assist the IASB to develop IFRS standards that are based on consistent concepts; (b) assist preparers to develop consistent accounting policies when no IFRS standard applies to a particular transaction or other event, or when a standard allows a choice of accounting policy;

objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity." Paragraph 2.4 of the Conceptual Framework adds: "*If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent.*" This objective is, in our view, entirely consistent with the concept of 'true and fair' as articulated in the Opinions, which focused on the need to satisfy the reasonable expectations of the readers to whom the accounts are addressed, those readers comprising "*businessmen, investors, bankers and so forth*".

(6) The Conceptual Framework also expands upon the meaning of 'faithful representation' at paragraphs 2.12 to 2.19, stating (at paragraph 2.13):

> "To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral and free from error. Of course, perfection is seldom, if ever, achievable. The Board's objective is to maximise those qualities to the extent possible."

It adds (at paragraph 2.16) that neutrality is supported by the exercise of prudence.[8] Again, this matches the approach taken in the Opinions which (as noted above) identified accuracy and comprehensiveness to within acceptable limits as two of the most obvious elements which contribute to a true and fair view.

38. In summary, therefore, the position is as follows:

(1) Financial statements prepared in accordance with UK-adopted international accounting standards must present fairly the financial position, financial performance and cash flows of an entity. This requires, amongst other things, the faithful representation of the effects of transactions, other events and

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and (c) assist all parties to understand and interpret the IFRS standards (see SP1.1 of the Conceptual Framework).

8 The reference to 'prudence' in the context of defining 'faithful representation' is significant, as its absence from an earlier iteration of the Conceptual Framework was one of the planks on which Mr. Bompas concluded that the international accounting standards might not admit the possibility of departure from their requirements even where those requirements resulted in accounts not giving a true and fair view. This was because he considered prudence to be the central principle entailed by the true and fair concept as applied to accounts (see paragraph 5.3 of his Opinion dated 8th April 2013).

conditions. The application of IFRS, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.

(2) Where management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the Conceptual Framework, paragraph 19 of IAS1 requires a departure from that requirement to ensure that the accounts do amount to a 'fair presentation'. Paragraph 20 requires the entity to disclose the adjustments that management has concluded would be necessary to achieve a 'fair presentation'.

(3) In the circumstances, it is clear to us that IAS1 does contain an override in favour of fair presentation, thus underlining the overarching nature of the requirement of fair presentation which (as noted above) is an articulation of the same concept as 'true and fair'. The existence of the override ensures that directors can comply with their duties under section 393(1) of the CA 2006 when preparing accounts in accordance with UK-adopted international accounting standards.

39. Accordingly, we consider that the view expressed by Mr. Moore in his 2008 Opinion as to the role of the 'true and fair' concept in the preparation of accounts (quoted above) remains accurate under English law.

Issue (4): whether, in reaching its view under regulation 7(1)(a), the UK Endorsement Board can assume that, if a specific standard is adopted, directors will retain the ability to reflect a true and fair view

40. As noted above, our view is that, on the current formulation of IAS1 as adopted for use in the UK, directors retain the ability to reflect a true and fair view of the assets, liabilities, financial position and profit or loss of the company in its financial statements, even where this would involve a departure from the relevant accounting standards; indeed, their duty under section 393(1) of the CA 2006 requires them to be satisfied that the accounts do give a true and fair view. If an addition or amendment to the international accounting standards were to deny directors the ability to prepare the accounts on the basis of a true and fair view, this would be a decisive factor against the adoption of the proposed addition or amendment in that form.

41. The existence of a true and fair override is of some (albeit limited) relevance to the UK Endorsement Board in the performance of its functions. The existence of the override

in IAS1 is a recognition that circumstances may arise in which compliance with the IFRS may result in accounts which do not give a true and fair view, albeit such circumstances will be "*extremely rare*". It follows that, as we observed above, in reaching the view that a proposed accounting standard is not contrary to the true and fair principle, the Board does not need to be satisfied that no circumstances could ever arise in which the application of the proposed standard would result in accounts which did not give a true and fair view, although it does need to be able to conclude that such circumstances would be "*extremely rare*".

42. However, and for the avoidance of doubt, the existence of a true and fair override does not enable the UK Endorsement Board to outsource the decision as to whether a proposed accounting standard is 'not contrary' to the true and fair principle to directors. The UK Endorsement Board is subject to a duty under regulation 7(1)(a) to reach its own view that the proposed standard is not contrary to the true and fair principle; and, as noted at paragraphs 20-1 above, in deciding whether the circumstances are such as to justify a departure from a UK-adopted international accounting standard, directors and the Court will attach significant weight to the fact that, following consultation with persons interested in the quality and availability of accounts, the UK Endorsement Board reached the view that the standard was not contrary to that principle.

Issue (5): whether, for the purposes of an assessment under regulation 7(1)(a), a standard should be considered in isolation or together with other previously UK-adopted standards

43. When considering whether a standard is 'not contrary' to the true and fair principle, the starting point for the UK Endorsement Board must be to consider the standard or amendment on its own terms. But this is not sufficient. A company preparing its accounts in accordance with the UK-adopted international accounting standards will not be preparing its accounts by reference to that standard alone, but by reference to the whole corpus of applicable standards. Therefore, when assessing a standard for the purposes of regulation 7(1)(a), it is important to assess the collective effect of the standards (as supplemented by the proposed new standard).

44. By way of analogy, when construing a contractual or a statutory provision, one looks not simply at the provision under scrutiny, but at the context in which the provision appears. Thus, in *Wood v. Capita Insurance Services Ltd.* [2017] A.C. 1173, S.C., on the correct approach to the interpretation of contracts, Lord Hodge JSC observed (at

[10]): "*It has long been accepted that this is not a literalist exercise focused solely on a parsing of the wording of the particular clause but that the court must consider the contract as a whole [...]*". The UK Endorsement Board should take a similar approach to the assessment of a proposed new standard.

Issue (6): whether the 'true and fair' test applies individually to assets, liabilities, financial position, profit and loss or to the collective effect of those items

45. The principle, as articulated in section 393(1) of the CA 2006 and regulation 7(1)(a) of the 2019 Regulations, is that the accounts must give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss. In the case of consolidated accounts, they must give a true and fair view of the assets, liabilities, financial position and profit or loss of the undertakings included in the accounts taken as a whole, so far as concerns members of the undertaking. For those preparing the accounts, however, it is of course necessary to consider such items in the context of the overall accounts.

46. Likewise, for the purposes of fulfilling its regulatory responsibility under regulation 7(1)(a), the UK Endorsement Board must reach the view that a proposed standard does not prevent accounts from giving a true and fair view in respect of any of the specific items identified in regulation 7(1)(a) when considered in the context of the preparation of the accounts as a whole.

Conclusion

47. We set out a summary of our conclusions on the issues on which we have been asked to advise above, at paragraph 3.

M. Neil Todd

Michael Todd Q.C.

Jack Rivett

Jack Rivett

Erskine Chambers

11th April 2022