Minutes of UKEB's Preparers Advisory Group meeting held on 31 October 2022 from 1.30pm to 5.00pm

Present	
Name	**Designation**
Pauline Wallace	Chair, UK Endorsement Board
Giles Mullins	Chair, PAG
Ben Binnington	PAG member
Cat Hoad	PAG member
Chris Buckley	PAG member
Ian Melling	PAG member
Jo Clube	PAG member
Luke Kelly	PAG member
Oliver Hexter	PAG member
Peter Leadbetter	PAG member
Stephen Morris	PAG member
Toby Odell	PAG member
Nick Anderson	IASB member
Nick Barlow	IASB staff

Paras Ali	IASB staff

Relevant UKEB secretariat team members were also present.

Welcome and Introduction

1. The Chair welcomed the Preparer Advisory Group (PAG) members and welcomed the two new members Peter Leadbetter and Ian Melling.

Endorsement: IAS 1 Presentation of Financial Statements 2020 and 2022 Amendment

2. The PAG considered a paper on two proposed amendments to IAS 1 in relation to the classification of debt as current or non-current. Specifically:

   a) The 2020 amendment clarifies requirements for classifying liabilities as current or non-current, and how lending conditions affected classification.

   b) The 2022 amendment addresses concerns with elements of the 2020 amendment, specifically around the impact of certain covenants on classification of liabilities.

   c) It was noted that some requirements in the final 2022 amendments had not been part of the original exposure draft.

   d) The amendments have an effective date of 1 January 2024.

   e) UKEB is responsible for adopting IASB standards and amendments before they can be used in the UK, according to criteria set out in the statutory instrument.

   f) A draft endorsement criteria assessment of the two amendments to IAS 1 is expected to be produced for discussion by the Board in February 2023, with publication for stakeholder comment expected shortly thereafter.

3. The following points were highlighted during the ensuing discussion:

   a) The PAG raised no specific concerns regarding the 2020 amendments, noting that the areas of concerns had been addressed by the 2022 amendments.

   b) With regard to the 2022 amendments, PAG members noted the following matters:

      i. Preparers felt the disclosures, with their requirement to consider the position of the company in relation to future covenant requirements, were indicative of a general trend that they were increasingly being asked to make predictions about the future.

ii. Materiality will be a key matter, and preparers feel the amendments could be quite subjective to apply.

iii. The amendments refer to 'loans with covenants' without defining the term 'loan'.

iv. Preparers would like a better understanding of how the requirements interact with going concern requirements in IFRS Standards.

v. The term "may have" in the new disclosure requirements (IAS 1 paragraph 76ZA(b)) could be open to wide interpretation if no threshold is provided.

vi. Large groups, with many loans across multiple jurisdictions are likely to have a wide range of different covenant requirements. Consolidating the loans across the group for appropriate disclosure of covenant requirements in group accounts could be difficult.

vii. Depending on the level of detail required (see concerns about materiality) the disclosure requirements could necessitate a lengthy note, that is disproportionate to the information it contains.

viii. Also, some of the information about covenants could be commercially sensitive.

ix. Alternatively, if the materiality threshold, and level of consolidation is at quite a high level, condensed and summarised disclosure could be so generic as to be worthless.

x. Auditors' interpretation of the requirements is currently outstanding.

xi. Some covenants are not necessarily as black and white as the requirements suggest, requiring significant judgement to make the appropriate assessments for disclosure.

Endorsement: Primary Financial Statements (roundtable discussion with the IASB project team)

4. The Chair welcomed the IASB's project team, including IASB Board member, Nick Anderson, and members of IASB staff. He noted that the Primary Financial Statements (PFS) project originated from investor demand for greater comparability between different sets of financial statements, more transparency

around non-IFRS performance measures, and strengthened disaggregation requirements

Statement of profit and loss subtotals and categories

5. The IASB project team summarised the exposure draft's (ED's) proposals and the IASB's subsequent tentative decisions on the proposed profit or loss categories of operating, investing and financing, highlighting the following points:

   a) The operating category is intended to capture income and expenses from an entity's main business activities, including volatile and unusual items.

   b) The investing category is intended to capture income and expenses from assets generating returns independently from other resources, share of profit or loss of equity accounted associates and joint ventures, and income and expenses on cash and cash equivalents.

   c) The financing category is intended to capture income and expenses on liabilities relating only to the raising of finance, and interest income on the unwind of the discount on other liabilities.

6. In the discussion the PAG raised the following points:

   a) There was concern about requiring income and expenses from cash and cash equivalents to be always captured in the investing category, given that cash may be held for operating and for financing purposes as well as for investing.

   b) Concern was expressed regarding the operating category with regard to entities in the UK insurance sector. It was stated that the proposals would result in operating profit volatility due to investment variance rather than due to how the business was managed. It was noted that European insurers typically reported fair value gains and losses through other comprehensive income and so would not suffer the same degree of operating profit volatility. While this is an outcome of IFRS 17 *Insurance Contracts* it was suggested the PFS proposals could exacerbate the matter.

   c) Concern was expressed regarding excluding the share of profit or loss of equity accounted associates and joint ventures from the operating category, as some felt that these investments formed part of an entity's main business activities and so their results should be included in the operating category. The IASB representatives noted that users had highlighted that an operating profit margin excluding share of profit of equity accounted associates and joint ventures aided comparability. The IASB representatives also noted that there was flexibility to use additional subtotals to present operating profit and share of profit of equity accounted associates and joint ventures.

Disaggregation

7. The IASB representatives highlighted the following:

   a) The proposals on disaggregation were designed to help entities decide when to present additional line items to provide an understandable overview of its income, expenses, assets, liabilities, and equity. Some items could be aggregated or disaggregated depending on whether the resulting information was material.

   b) The ED proposed that entities presenting operating expenses by function in the statement of profit or loss should disclose an analysis of operating expenses by nature in the notes. Feedback to the ED had highlighted that this analysis would be too costly for some entities to provide. The IASB has therefore taken a tentative decision to explore a requirement to disclose the amount of depreciation, amortisation, and employee benefits in each functional line item, to achieve a balance between cost and benefit. The IASB is also considering expanding this requirement to include impairments and inventory write downs, or to expand it to include any expense items separately disclosed in the financial statements.

8. The discussion raised the following points:

   a) There was strong concern amongst preparers regarding the cost of implementing the ED's proposal to require an analysis of operating expenses by nature in the notes when operating expenses were presented by function in the statement of profit or loss.

   b) Amounts of depreciation, amortisation and employee costs absorbed into inventory would not necessarily be required to be analysed by nature, although such an analysis is required in some jurisdictions.

   c) There was a call for re-exposure of proposals regarding analysis of operating expenses by nature, given that the IASB's tentative decisions since the consultation on the ED were different to the proposals in the ED.

   d) Depreciation, amortisation, and employee costs might not always be the most relevant costs to analyse by functional category. Other expenses, for example, raw materials, might be more relevant.

   e) The IASB representatives noted that users understood the need for balance between added costs and additional information disclosure.

   f) Expanding the list of expenses to be analysed by functional category could reduce levels of voluntary disclosure as entities may stop disclosing expenses they do not want to analyse by functional category

g) The IASB representatives noted that investors who were aware of the project were comfortable that they would be able to access the information they wanted. Information such as employee costs were increasingly important, while depreciation and amortisation provided a stronger link with cash flow.

Management Performance Measures (MPMs)

9. The IASB representatives highlighted the following:

   a) The ED proposed defining a subset of non-GAAP measures as MPMs and requiring certain disclosures about them. MPMs were defined in the ED as subtotals of income and expenses that are used in public communications outside financial statements, complement totals or subtotals specified by IFRS standards, and communicate management's view of an aspect of an entity's financial performance.

   b) The key disclosure requirements included reconciliation of MPMs with the closest subtotals in IFRS; an explanation of how MPMs were calculated and how the information was useful; and an explanation of any changes in the method of calculation and the impact of those changes on the MPM. Disclosure requirements also included the impact on tax and non-controlling interest (NCI) of any reconciling items in the reconciliation of MPMs to directly comparable subtotals in IFRS.

   c) The proposals were strongly supported by stakeholders although the IASB has taken some tentative decisions which differ from the proposals in the ED to reflect feedback on potential application questions.

   d) The IASB has taken a tentative decision to include a rebuttable presumption that a MPM communicated management's views of an entity's performance, to ensure that measures do not fall out of scope on the grounds that they do not communicate managements views of an entity's performance.

   e) The IASB has taken a tentative decision to allow a simplified approach to calculating the tax and NCI impact of reconciling items between MPMs and the closest IFRS subtotal.

10. In discussion the following points were raised:

   a) The proposals could cause confusion about which measures used by management to measure performance fall within scope.

   b) Management performance measures in the UK do not tend to include tax effects and effects of non-controlling interests. Some PAG members believed that users prefer measures which are post-tax and at EPS level in order to interrogate the management performance number and assess the validity of reconciling items. It was noted that the tax expense in the statement of profit or loss might not be the same as the cash tax payable, and that the cash tax payable may be of more interest to users.

c) Feedback to the ED had questioned whether the scope of the measures should be expanded beyond items of income and expense, to include the balance sheet and statement of cashflows, but the IASB had tentatively decided to restrict the definition to subtotals of income and expense.

Research: Accounting for Intangibles

11. The UKEB Secretariat provided an update to the PAG members on the UKEB's Intangibles Research Project.

a) It is one of the three projects added to the IASB's work plan as a result of the IASB Third Agenda Consultation.

b) The UKEB is undertaking a project to understand perspectives on the accounting for intangibles from UK stakeholders' and possible ways to enhance the accounting for intangibles.

c) Intangibles are recognised as important source of economic growth and are growing significantly. According to ONS surveys, approximately £670bn of intangibles are present in the UK economy but are largely unreported in companies' financial statements.

d) In 2022, the UKEB agreed to conduct a multi-output, proactive research project on intangibles. Currently, the UKEB is finalising the qualitative research that includes interview-based research setting out UK stakeholder views on accounting for intangible assets.

e) Simultaneously, the UKEB has also begun quantitative analysis of the intangible reporting in the UK, considering both largest and a sample of companies across the reporting landscape. Following on from this, the UKEB will carry out a user survey.

12. The Secretariat noted that the following common issues were emerging during this phase of research:

a) Limited recognition of intangibles

b) Inconsistent accounting treatment

c) Poor disclosures

13. The Secretariat put the following questions to Advisory Group members:

a) What, if anything, is wrong with the accounting under IAS 38 Intangible assets?

b) What could be done to improve the accounting for intangibles?

14. PAG members highlighted the following points of note and problems with IAS 38:

a) IAS 38 Intangible Assets entails a high threshold for recognition that does not allow many types of assets to be recognised on companies' balance sheets. However, some PAG members did not necessarily see this as a problem, for example because of the difficulty in attributing future economic benefits to intangible assets or because they are difficult to identify and evaluate individually, especially among smaller businesses.

b) IAS 38 disclosures are relatively limited, on assets and expenses alike.

c) Different treatment of internally generated intangible assets under IAS 38 and assets acquired in a business combination in IFRS 3 could have a "behavioural impact" on companies' management, such as giving an incentive to grow by acquisition or selectively embark on projects according to what could be recognised on the balance sheet. This could lead to management's judgements and inconsistencies between companies' accounts.

15. PAG members discussed the following potential solutions to the problems:

a) One PAG member noted that the recognition criteria of IAS 38 could be relaxed to allow companies to recognise internally generated brands and employment/training costs. In particular, they noted training to deliver a specific contract should be capitalised. Two PAG members however disagreed with this view, suggesting that there may be inconsistencies between companies and issues with the accuracy of those estimates.

b) However it was noted that differentiating between capital expenditure and actual investment is sometimes tricky, and in fact companies may have an incentive to capitalise in order to keep capital expenditure as low as possible.

c) One PAG member noted that accrual accounting could be meaningless for insurance companies and other financial institutions, as users wanted to know what was being spent and when it would have returns.

d) With reference to brands, one PAG member noted that the entirety of operations may in theory contribute to supporting its brand value, so how does one identify what expenses should be capitalised?

e) It was noted that consideration might be needed for recognition of intangibles among transnational companies, for example how can an intangible such as a global brand be broken up geographically?

f) Fair value measurement for intangibles was also discussed, with PAG members suggesting that fair value could be more appropriate for particular types of intangibles. A PAG member noted that for brands what matters is the fair value of the brand, rather than the capitalisation of its annual expenditure to maintain brand awareness. PAG members emphasised that fair value may be needed by users, though one member raised the point that valuation methodologies were complex and would need to be assessed by auditors.

g) PAG members noted that enhancing disclosures for intangibles may be a viable solution. However, a PAG member noted that companies may be concerned about the commercial sensitivity leading to limited disclosure being provided.

Horizon Scanning

16. The Chair noted that the Board had recently considered the impact of changing economic conditions, including interest rates and inflation. He invited members' input on what PAG should consider in relation to this topic.

17. The following points were highlighted by PAG members:

a) The changing economic conditions posed a number of challenges for the insurance industry, such as the disclosure of changes to premiums/ payouts, and the need to lock in financial assumptions at the start of a contract. This can be difficult and not necessarily lead to useful information. The industry was likely to share this feedback during the IFRS 17 Insurance Contracts post-implementation review.

b) Consideration of the ways to measure inflation rates and incorporate into future estimates was ongoing. Some suggested it may be helpful if accounting standards could do more assist with such judgements. It was noted that higher inflation created greater volatility/differences between company results, particularly between those capitalising costs and those that did not.

c) A PAG member noted that they had provided additional disclosure about the split of assets in pension schemes. It was observed that pension schemes had inherent risks – assets may be declining, while liabilities were being discounted. Currency issues such as the current strength of the dollar also influence this.

18. PAG members shared concerns regarding IASB and ISSB interaction. The basis of measurement could sometimes differ between the IFRS accounting standards and the ISSB's standards. It was possible for a disconnect to develop between disclosures and the intentions driving them. PAG members also observed that the ISSB appeared to be moving more rapidly than the IASB, which has the potential to further exacerbate such interactions.

Endorsement: Approach to the Economic Impact Assessment (Narrow Scope Amendments).

19. The UKEB's proposed approach to the Economic Impact Assessment for endorsing narrow scope amendments was presented which highlighted:

    a) The narrow scope amendments are typically not expected to have a high impact on the economy, and in such cases it is proposed to standardise the process as much as possible.

    b) A standardised cost model was crucial to this, and would enable calculation of preparers' compliance costs and understand expected benefits.

    c) This would enable the secretariat to calculate average cost of compliance for narrow scope amendments without project-by-project stakeholder engagement on this aspect.

    d) A survey was expected to be carried out with preparers, and updated every three to five years. The initial survey was due to take place in the first quarter of 2023.

    e) Volunteers were requested from the PAG to pilot the survey prior to release.

AOB

20. The UKEB Chair invited PAG members to provide feedback on the agenda and meeting format.

21. A PAG member was provided with information on engaging with UKEB to discuss the primary financial statements project.

22. The Chair noted that the next meeting would take place on 6th February 2023.

23. There being no other business, the meeting closed at 17.00.