

2005 No. 2210

FRIENDLY SOCIETIES

**The Friendly Societies (Accounts and Related Provisions)
(Amendment) Regulations 2005**

<i>Made</i> - - - -	<i>4th August 2005</i>
<i>Laid before Parliament</i>	<i>8th August 2005</i>
<i>Coming into force</i> - -	<i>1st October 2005</i>

The Treasury, in exercise of the powers conferred upon them by sections 70 and 71 of the Friendly Societies Act 1992(a) hereby make the following Regulations:

Citation, commencement and interpretation

1.—(1) These Regulations may be cited as the Friendly Societies (Accounts and Related Provisions) (Amendment) Regulations 2005.

(2) These Regulations come into force on 1st October 2005 and have effect as respects financial years which begin on or after 1st January 2005 and end on or after October 2005.

(3) In these Regulations—

- (a) “the principal regulations” means the Friendly Societies (Accounts and Related Provisions) Regulations 1994(b);
- (b) references to numbered schedules are to schedules to the principal regulations.

Miscellaneous amendments to the principal regulations

2.—(1) The principal regulations are amended as follows.

(2) In regulation 2(1) (interpretation), for “section 69” wherever occurring, substitute “section 69E”.

(3) In regulation 7 (group accounts – supplementary provisions)—

- (a) in paragraph (3), for “subsections (2) and (3) of section 70” substitute “subsection (2) of section 69F”;
- (b) in paragraph (7), for “subsections (2) and (3) of section 70” substitute “subsection (2) of section 69F”.

(4) After regulation 10 (accounting principles and rules), insert the following—

(a) 1992 c. 40

(b) S.I. 1994/1983, amended by S.I. 2001/3649.

“Accounts to have regard to substance of a transaction

10A. The management committee of a society shall, in determining how amounts are presented within items in the income and expenditure account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.”

(5) In Schedule 2, in the Balance Sheet Format under the heading Liabilities, for “Provisions for other risks and charges” substitute “Provisions for liabilities”.

(6) In paragraph 19(1)(b) of Schedule 4 (reserves and provisions) and in paragraph 19(1)(c) of Schedule 4 (reserves and provision) for “provisions for liabilities and charges” substitute “provisions for liabilities”.

(7) In sub-paragraph 4(b) of Schedule 6 omit “and losses” and “ or are likely to arise”.

Information about fair value in notes to the accounts

3. After paragraph 32 of Schedule 5 (notes to the annual accounts), insert—

“Information about fair value of assets and liabilities

33.—(1) This paragraph applies where financial instruments have been valued in accordance with paragraph 24A or 24C of Schedule 6.

(2) There shall be stated in the notes to the accounts –

- (a) the significant assumptions underlying the valuation models and techniques used where the fair value of the instruments has been determined in accordance with paragraph 24B(4) of that Schedule;
- (b) for each category of financial instrument, the fair value of the instruments in that category and the changes in their value –
 - (i) included in the income and expenditure account, and
 - (ii) credited to or (as the case may be) debited from the fair value reserve,in respect of instruments in that category; and
- (c) for each class of derivative financial instruments, the extent and nature of the instruments, including significant terms and conditions that may affect the amount, timing and certainty of future cash flows.

(3) Where any amount is transferred to or from the fair value reserve during the financial year, there shall be stated in tabular form –

- (a) the amount of the reserve as at the date of the beginning of the financial year and as at the balance sheet date respectively;
- (b) the amount transferred to or from the reserve during that year; and
- (c) the source and application respectively of the amounts so transferred.

(4) Where investments are shown at their purchase price, their fair value shall be disclosed in the notes on the accounts.

(5) Where investments are shown at their fair value, their purchase price shall be disclosed in the notes to the accounts.

(6) The valuation method applied to each investment item shall be stated in the notes to the accounts, together with the amounts so determined.

Information where investment property or living animals and plants included at fair value

34.—(1) This paragraph applies where the amounts to be included in a society’s accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 24D.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts –

- (a) the comparable amounts determined according to the historical cost accounting rules; or
- (b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to –

- (a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and
- (b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or required in determining those amounts according to those rules.”.

Valuation at fair value

4.—(1) Schedule 6 is amended as follows.

(2) In paragraph 8(1)(a) (preliminary) for “must be determined in accordance with that paragraph” substitute “may be determined in accordance with that paragraph or with paragraphs 24A, 24C or 24D”.

(3) In paragraph 8(1)(b) at the end insert “or with paragraphs 24A, 24C or 24D”.

(4) In paragraph 9 at the end insert, “or shown as assets under CI in the balance sheet”.

(5) In paragraph 12(2) for “above” substitute, “,24A, 24C or 24D,”.

Fair value method of valuation for assets

5. At the end of Part IV of Schedule 6, insert—

“Part IVA

Valuation at Fair Value

Inclusion of financial instruments at fair value

24A.—(1) Subject to sub-paragraphs (2) to (4), financial instruments, including derivative financial instruments, may be included at fair value.

(2) Sub-paragraph (1) only applies to financial instruments which constitute liabilities if –

- (a) they are held as part of a trading portfolio; or
- (b) they are derivative financial instruments.

(3) Sub-paragraph (1) does not apply to –

- (a) non-derivative financial instruments held to maturity;
- (b) loans or receivables originated by the society and not held for trading purposes;
- (c) interests in connected undertakings or joint ventures;
- (d) equity instruments issued by the society;
- (e) contracts for contingent consideration in a business combination; and
- (f) other financial instruments with such special characteristics that the instruments, according to generally accepted accounting principles or practice, should be accounted for differently from other financial instruments.

(4) If the fair value of a financial instrument cannot be determined reliably in accordance with paragraph 24B, sub-paragraph (1) does not apply to that financial instrument.

(5) In this paragraph “joint venture” means an undertaking, other than a connected undertaking, which a society manages jointly with one or more undertakings.

Methods for determining “fair value”

24B.—(1) The fair value of a financial instrument is its value determined in accordance with this paragraph.

(2) If a reliable market can readily be identified for the financial instrument, its fair value is to be determined by reference to its market value.

(3) If a reliable market cannot readily be identified for the financial instrument but can be identified for its components or for a similar instrument, its fair value is to be determined by reference to the market value of its components or of the similar instrument.

(4) If neither sub-paragraph (2) nor (3) applies, the fair value of the financial instrument is to be a value resulting from generally accepted valuation models and techniques.

(5) Any valuation models and techniques used for the purposes of sub-paragraph (4) must ensure a reasonable approximation of the market value.

Hedged items

24C. A society may include any assets or liabilities, or identified portions of such assets or liabilities, which qualify as hedged items under a fair value hedge accounting system, at the amount required under that system.

Other assets which may be included at fair value

24D.—(1) This paragraph applies to—

- (a) investment property; and
- (b) living animals or plants,

that under international accounting standards may be included in accounts at fair value.

(2) Such investment property and such living animals or plants may be included at fair value, provided that all such investment property, or as the case may be, all such living animals or plants are so included where their fair value can be reliably determined.

(3) In this paragraph “fair value” means fair value determined in accordance with relevant accounting standards.”

Accounting for changes in value of financial instruments

24E.—(1) This paragraph applies where a financial instrument is valued in accordance with paragraph 24A or 24C.

(2) Notwithstanding paragraph 4 of Part I of this Schedule, and subject to sub-paragraphs (3) and (4) below, a change in the value of the financial instrument shall be included in the income and expenditure account.

(3) Where—

- (a) the financial instrument accounted for is a hedging instrument under a hedge accounting system that allows some or all of the change in value not to be shown in the income and expenditure account; or
- (b) the change in value relates to an exchange difference arising on a monetary item that forms part of a society’s net investment in a foreign entity,

the amount of change in value shall be credited to or (as the case may be) debited from a separate reserve (“the fair value reserve”).

- (4) Where the instrument accounted for—
 - (a) is an available-for-sale financial asset; and
 - (b) is not a derivative financial instrument,

the difference in value may be credited to or (as the case may be) debited from the fair value reserve.

The fair value reserve

24F.—(1) The fair value reserve shall be adjusted to the extent that the amounts shown in it are no longer necessary for the purposes of paragraph 24E (3) or (4).

(2) The treatment for taxation purposes of amounts credited to or debited from the fair value reserve shall be disclosed in a note to the accounts.”.

Amendment of Schedule 9

6.—(1) Schedule 9 (interpretation of schedules) is amended as follows.

(2) In paragraph 7(3) (provisions)—

- (a) omit “and charges”;
- (b) for “or loss” substitute “the nature of which is clearly defined and”.

(3) In paragraph 10 (other definitions), before the definition of “fungible assets”, insert—

““fair value reserve” has the meaning given by paragraph 24D of Schedule 6;”.

(4) After paragraph 10, insert –

“Financial instruments

11. References to “derivative financial instruments” are deemed to include commodity-based contracts that give either contracting party the right to settle in cash or some other financial instrument, except when such contracts –

- (a) were entered into in order to meet the society’s expected purchase, sale or usage requirements and continue to meet those requirements;
- (b) were designated for such purpose at their inception; and
- (c) are expected to be settled by delivery of the commodity.

Further Expressions

12.—(1) The expressions listed in sub-paragraph (2) have the same meaning as they have in Council Directive 78/660/EEC (a), and for the purposes of those expressions, it shall be assumed that a society is subject to the provisions of that Directive.

(2) “Available-for-sale financial asset”, “business combination”, “cash flow risk”, “commodity-based contracts”, “credit risk”, “equity instrument”, “exchange difference”, “fair value hedge accounting system”, “financial fixed asset”, “financial instrument”, “foreign entity”, “hedge accounting”, “hedge accounting system”, “hedged items”, “hedging instrument”, “held to maturity”, “held for trading purposes”, “liquidity risk”, “monetary item”, “price risk”, “receivables”, “reliable market” and “trading portfolio”.”.

*Dave Watts
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4th August 2005

Two of the Lords Commissioners of Her Majesty’s Treasury

(a) OJ L 222, 14.8.1978, p. 11; as amended by Council Directive 83/349/EEC, Council Directive 84/569/EEC, Council Directive 89/666/EEC, Council Directive 90/604/EEC, Council Directive 90/605/EEC, Council Directive 94/8/EC, Council Directive 1999/60/EC and European Parliament and Council Directive 2001/65/EC.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations make provision to give effect to parts of Directive 2003/51/EC of the European Parliament and of the Council amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC as regards modernising the annual and consolidated accounts of certain types of companies, banks and other financial institutions to bring the preparation of those accounts more into line with international accounting standards (OJ L 178, 17/07/2003, p.16 – 22) (“the Modernisation of Accounts Directive”);

The parts of the Modernisation of Accounts Directive implemented by these Regulations are those which require amendments to be made to the Friendly Societies (Accounts and Related Provisions) Regulations 1994 (S.I. 1994/1983 – “the 1994 Regulations”).

The Regulations also change cross-references to sections of the Friendly Societies Act 1992 required by the Friendly Societies Act 1992 (International Accounting Standards and Other Accounting Amendments) Order 2005.

Regulation 2 makes several amendments required to implement the Modernisation Directive, including a new requirement for committees of management to have regard to the substance of a transaction when determining how amounts are presented.

Regulations 3, 4 and 5 make provision for societies to use fair value to value some of their assets and to disclose in their notes certain matters where they use fair valuation methods.

Regulation 6 amends schedule 9 to the 1994 Regulations which contains definitions for terms used in the schedules to the 1994 Regulations.

A transposition note showing how the main provisions of the Modernisation Directive (as it applies to friendly societies) will be transposed into UK law is available from HM Treasury. Copies may be obtained from the General Insurance, Mutuels and Inclusion Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ and the notes will be available on the Treasury website (www.hm-treasury.gov.uk).

A regulatory impact assessment has been prepared in relation to these Regulations. A copy of it is available on the Treasury website or from the above address. Copies of the transposition note and the regulatory impact assessment have been placed in the library of both Houses of Parliament.