

MINUTES OF THE 83rd FRAB MEETING HELD ON MONDAY 11th DECEMBER 2006 AT HM TREASURY

Present: Elwyn Eilledge (Chair)
Kirstin Baker
Miranda Carter
Russell Frith
Robin Lynch
Owen Mason
Peter Ryland
Martin Sinclair
John Thornton
Ken Wild

Ian Carruthers
Simon Fiander
David Heald
Ian Mackintosh
Alastair Matthews
Anne Rylatt
David Thomson
Steve Warren

Secretariat: Larry Pinkney (Secretary)
Sarah Solomon
Christine Ruston

1. The Chairman welcomed everyone to the meeting. Apologies were received from Christine Daws (who was substituted for by Peter Ryland), Martin Evans (substituted for by Steve Warren), Robert Ffello (substituted for by Simon Fiander) Nigel Reader (substituted for by Owen Mason), Alyson Stafford (substituted for by Scott McKay), Jeff Tomlinson (substituted for by Anne Rylatt) and Trevor Woolley (substituted for by John Thornton).
2. The Chairman welcomed Ian Mackintosh whose appointment as ASB nominee to replace Mike Ashley has been confirmed by the Comptroller and Auditor General.

Item 1: Minutes of the Last Meeting: Paper FRAB (83)01 and Matters Arising

3. The minutes of the last meeting were agreed subject to the following amendments:
 - In paragraph 20 “phase 9” should be amended to “phase G”
 - In paragraph 27 “recommendations” should be amended to “proposals”
 - In paragraph 29 “an SPV” should be amended to “a project”
 - The last sentence of paragraph 36 should be amended to read “The Treasury will reconsider the issue, including considering whether the first opening IFRS balance sheets should be published (although there did not seem to be any support for

publication within the FRAB), and switching the emphasis in the FReM amendment to one of using IFRS based comparative figures.”

4. The Treasury confirmed that they had informed departments via the FRAB minutes produced from previous meetings and issued through the RABIG network that the FRAB may recommend withdrawal of the Technical Note.

Item 2: Oral Update on Whole of Government Accounts (FRAB(83)02)

5. Kieran Rix gave an update on the progress of the Whole of Government Accounts Programme. The Board was last updated just after the 2005 PBR in which the document “Delivering the Benefits of Accruals Accounting” had been issued. The document highlighted the major challenges that faced the programme. The biggest risk was the local government convergence process. The number of local authorities producing group accounts had increased and this was welcomed. There is some evidence in the WGA data that not all authorities have provided their group accounts. However it was acknowledged that a risk remained since Local Authorities often struggled in the first year of SORP changes and it was hoped this would be resolved in 2007.
6. The principal challenge of convergence is the valuation of local Authority infrastructure. A working group has been set to look into the desirability and practicality of converging on the local authority and central government treatments. The working group includes a wide coalition of people including the engineering profession who are keen to drive progress forward.
7. There are other challenges around those public corporations which are currently not applying modified historic cost accounting. However the initial view is that on the basis of 04-05 information most of the material is available to provide modified historic cost. There is still a risk that the valuations could become out of date; this is not expected to be a big problem; but the WGA Team are keeping this under review.
8. The move to IFRS is also an issue and the HMT work on the IFRS FReM will provide a basis for WGA.
9. A bigger issue is what happens outside central government, in particular, local government, where those in the field may consider WGA less of a priority. Ian Carruthers said that CIPFA had begun to track this process and the implications on the SORP, but so far there were no major changes. He also said that the majority of comments on the 2007 SORP Invitation to Comment were concerning financial instruments and that there was a residual problem around soft loans.

10. The Treasury feels that they have a contribution to make in terms of helping Local Authorities to prepare for change. Treasury will be responsible for possibly the largest consolidation with the three largest sub-sectors being in central government.
11. Kieran gave a summary of the 2004-05 process and talked about the outcomes. 2004-05 was the first year that local authorities, NHS Trusts and Foundation Trusts were included. The NHS provided a high quality return, however it was disappointing that for central government there was a drop in quality and timeliness. It was clear that this was partly as a result of bringing the timetable forward and also because of the pressures of faster closing. There has always been some inconsistency between Departments' WGA returns and their resource accounts, some due to different rules, some due to mistakes. Greater consistency in accounting practice in 2006-07 should mean improvements. There was a disappointing level of returns for local government which meant that there weren't enough for a full consolidation. There was also a variety of interpretations of the SORP and the Treasury is working towards a programme of work to address this. (Peter Ryland asked to ensure that Audit Wales and Audit Scotland were included in discussions.)
12. In 2005-06 there were further developments in the process, including audited returns for local government, unaudited WGA returns for public corporations, an advanced timetable for central government and a new dry run segmental reporting approach. Further issues emerged including ensuring better quality and timeliness of both central government and local government returns. Transactions between central and local government remain a major issue, as does diversity of accounting practice. Although different issues apply in different sectors.
13. Plans for 2006-07 include working on sub consolidations to make the process smoother, working with CIPFA on the application of the SORP and working with the new Treasury Accountant to achieve consolidated management accounting for the central funds. The Treasury is also working on the integration of WGA data into fiscal policy which has already led to policy work based on the data.
14. It was reported that the timetable for departmental WGA returns was being brought forward. David Heald asked about when published audited WGA can be expected, and what trade off there was in bringing the timetable for returns forward. The timetable for publication of WGA remains as announced (i.e. a published balance sheet for 2006-07, subject to resolving outstanding issues) and that although there had been an effect on the quality of WGA returns, the intention was to keep the pressure on in terms of advancing the WGA timetable whilst improving the quality.
15. Russell Frith asked about the infrastructure group and the need to get a link to depreciation in the figures. Kieran confirmed that Department for Transport were included in the group.

Item 3: PFI – Update on Progress (FRAB(83)03)

16. The Treasury presented this paper which formalised what was reported orally at the last meeting and outlined the actions taken since then. It was reported that there had been discussion of PFI accounting issues within Treasury and what the impacts might be, including beyond accounting implications, should Ministers decide to withdraw the Technical Note (TN).
17. Treasury reassured the Board that its views on PFI accounting were being taken seriously and acknowledged that it would be unprecedented for the Treasury not to follow the Board's advice should the Board make formal recommendations. Nonetheless, final decisions would be for Ministers.
18. It was reported that although the PFI Working Group is likely to recommend the withdrawal of the TN to the Board, it was also asked to consider whether there should be any interpretative guidance related to Application Note F to FRS 5 contained within the FReM. This issue is yet to be considered by the PFI Working Group and it was acknowledged there was a risk that including further guidance within the FReM could create similar inconsistencies to that experienced in relation to the application of the TN.
19. It was also reported that the IASB has issued the IFRIC on Service Concessions and IPSASB have set up a working group to consider a public sector standard. The Treasury would need to take account of these developments in considering future PFI accounting guidance.
20. Kirstin Baker added that any accounting changes could impact on budgeting and service delivery. Previously the Board had discussed timing the changes to coincide with the forthcoming CSR. This was not a relevant consideration as CSR guidance had already been issued to departments and the basis for capital allocations was clearly understood. It was more important to fully consider the implications of any changes and HMT Ministers would need time to do that. Departments should be clear that the status quo would continue until such time as Ministers decided otherwise.
21. Martin Sinclair was keen that the PFI Working Group met again as soon as possible. David Heald felt that it would be important to include the specimen PFI case studies that had been discussed by the Working Group in its final report and that Treasury should address the timing element in its next report to the Board. He was surprised at the emphasis on the views of the firms, rather than those of public audit bodies and requested that the public audit bodies view be made clear in the future update to the Board.
22. There will be one further meeting of the Working Group before it reports back to the Board in February. The Board was informed that it can expect two PFI papers at the next FRAB meeting: one from the PFI

Working Group representing its final report, the other from the Treasury to provide context. The Board requested that the Treasury paper cover the issue of timing. The two papers will be developed in parallel.

23. The Chairman thanked the Treasury for the update and acknowledged that there is clearly some related work going on within Treasury, but expressed the view that the Board was as concerned as ever on PFI. He acknowledged that the ramifications of any potential changes extended beyond accounting and expressed his concern that there needs to be a comprehensive response from Treasury at the next meeting.

Item 4: IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors (FRAB(83)04)

24. The Treasury introduced this paper which recommended that IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, should apply in full in the IFRS based FReM. This Standard covers the same ground as its equivalents in UK GAAP (FRS 18 Accounting Policies and FRS 3 *Reporting Financial Performance*).
25. There are several differences, including some relating to the correction of errors. Unlike FRS 3, IAS 8 provides guidance on the circumstances under which retrospective application of changes in accounting policy or the correction of errors is impracticable. IAS 8 requires that all material errors be retrospectively corrected. FRS 3 defines a fundamental error as being of such significance as to destroy the true and fair view of the financial statements. IAS 8 states that errors are material if they could individually or collectively influence the economic decisions of users. It therefore appears to set a lower threshold for the correction of prior period errors than does FRS 3.
26. The Board agreed that IAS 8 should be adopted without interpretation.
27. Steve Warren commented that the Standard will involve more work at consolidation of accounts and that it would influence the True and Fair View in conducting audit.

Item 5: Common Control – Application in the Public Sector (FRAB (83)05)

28. The Treasury presented this paper which outlined the Treasury's approach to common control and its alignment to ONS classifications, as a result of previous discussions on NHS Foundation Trusts - Accounting for Mergers and Acquisitions at the last meeting (FRAB (82) 10). The paper outlined that in applying FRS 6, the Treasury takes the ONS classification of the public sector body as forming the boundary of general government's common control. In its view Foundation Trusts are under general government common control and combinations involving these trusts should be merger accounted in compliance with the FReM.

29. Miranda Carter reiterated Monitor's position that in certain circumstances combinations of an NHS Trust with a Foundation Trust (FT), or a FT with another FT, should be accounted for using acquisition accounting. This view is based on FTs having far greater freedom than NHS Trusts and are largely free of the control of the Secretary of State.
30. The Chairman commented that it would be counter-intuitive to form the view that FTs are not under common control.
31. Ian Mackintosh suggested that the changes associated with the suggested treatment for acquisition accounting wouldn't have a large effect. Miranda commented that Monitor was aiming to reflect a true and fair view in the accounts of FTs and felt that many transactions between FTs and NHS trusts could have the substance of an acquisition. She requested a divergence from the FReM to allow acquisition accounting at the FT level but commented that this could be adjusted out at the whole of government accounts level.
32. Martin Sinclair commented that the suggested proposal by Monitor would make an unnecessary divergence and supported the HM Treasury view.
33. The Board further discussed and accepted the Treasury's approach on common control but recognised that FTs were close to the boundary. However, Monitor's proposal for acquisition accounting was not supported by the Board as it was considered an unnecessary divergence which would have marginal effects.

Item 6: IAS 24: Related Party Disclosures (FRAB(83)06)

34. The Treasury presented this paper which considered the application of IAS 24 in the IFRS based FReM. The proposed interpretations of IAS 24 are intended to retain the same level of disclosure as currently disclosed under FRS 8. The proposals include the following interpretations:
- Disclosures of transactions with related parties, other than with individuals, may be restricted to the name of the entity's parent department and a note of the main entities within government with which the entity has had dealings;
 - Charities follow the requirements given in the charities SORP;
 - The requirement to disclose e.g. compensation paid to management is included in the disclosures given in the Remuneration Report;
 - The proposed amendment notes that the definition of materiality in IAS 1 means that the effect of a related party transaction should be judged from the viewpoint of both the entity and of the individual; and

- Ministers (including members of their close family) are not regarded as related parties. This has been the subject of ongoing discussions. At the moment the proposed amendment to the FReM doesn't include anything on ministers.
35. The Treasury has consulted Australia and New Zealand on the differences in applying IAS 24 rather than FRS 8. New Zealand specifically excludes ministers from the scope of IAS 24 and while Australia doesn't include ministers at the moment, it is considering including them in the future. The Treasury is taking forward discussions on this issue and is planning to consult ministers. It plans to resubmit a paper to the Board in March.
36. Ken Wild felt that the paper should include argument around whether ministers should be regarded as related parties based on the definitions in IAS 24. He also felt that it would also be helpful to consult with China.
37. Martin Sinclair reminded the Board of the previous discussion where it had agreed that ministers are related parties. He felt that this remained the Board's position in principle. He advised that although the NAO in principle see ministers as related parties, he noted the Treasury decision to exclude guidance on ministers and agreed that the Board should defer any decision until the Treasury had undertaken further research and reported further.
38. However other members of the Board felt that a clear message should be sent to ministers that they should not be excluded from the disclosures and that the Board felt that refusal to do so was a risky position to take.
39. Ian Mackintosh suggested that in the proposed amendment the bullet related to materiality should be removed, in that materiality is not an issue as there is a need to show all transactions. Anne Rylatt suggested that "other government departments and other central government bodies" in the third paragraph of the draft Annex should be amended to read "other government bodies".
40. The Chairman confirmed that the Board presumes that ministers are related parties as per IAS 24, pending further HM Treasury work on this issue, and that the IFRS based FReM should reflect this.
41. The Treasury would amend the proposed wording in the IFRS based FReM, continue its work and report back to the Board in March.

Item 7: IFRS 1: First Time Adoption of International Financial Reporting Standards (FRAB(83)07)

42. The Treasury presented a paper at the last meeting which proposed that the first set of IFRS-based accounts might include UK-GAAP based comparative figures unless there were material differences between figures determined on a UK-GAAP and IFRS basis.

Comments from many of the Board members at the last meeting suggested that there was no sound reason to do this and the Treasury was asked to reconsider the emphasis in the paper and resubmit it . The revised paper reflects the change in Treasury's position, which now concurs with the Board's view, and proposed that the IFRS be applied in full . The Board agreed the suggested amendment to the IFRS based FReM.

Item 8: Amendments to the FReM in Respect of the Preparation of the Remuneration Report (FRAB (83)08)

43. At the September meeting FRAB (81)07 it was reported by HM Treasury that a number of NDPBs with charitable status were not complying with the FReM in respect of salary and pension disclosures, as the Remuneration Report containing the disclosure forms part of the Annual Report in the FReM, and charitable NDPBs are not required to produce an Annual Report, but instead produce a Trustees' Report. The Treasury presented this paper which proposed amendments to the 2006-07 FReM to clarify that NDPBs with charitable status should prepare a Remuneration Report.
44. The Board agreed the suggested amendments.

Item 9: SSAP 5: Accounting for Value Added Tax (FRAB (83)09)

45. The Treasury presented this paper which recommended that SSAP 5 (as interpreted for the public sector context), which has no equivalent International Financial Reporting Standard, should continue to apply in full in the IFRS based FReM, to those entities subject to the tax regime.
46. The Board agreed that the interpretation of SSAP 5 should be carried over to the IFRS based FReM.

Item 10: IAS 18: Revenue (FRAB (83)10)

47. The Treasury presented this paper which recommended that IAS 18 should be adopted in full as interpreted for the public sector context, in that only realised profits be included in the profit and loss account.
48. It was noted that the IASB/FASB are working to develop a new International Accounting Standard on revenue recognition, replacing IAS 18. Preliminary views are not due until the second quarter of 2007, however early work suggests the approach is consistent with that of UK GAAP (Application Note G) rather than the current IAS 18).
49. IAS 18 allows, but does not require, unrealised profits to be included in the profit and loss account. This in general is not consistent with National Accounts or the budgeting and Estimates regime. Therefore the Treasury recommended that IAS 18 be interpreted. The Treasury reported that the treatment of unrealised profits in other Standards will depend on their interpretation or adaptation for the public sector

context. The Treasury felt that the move to IAS 18 with the suggested interpretation is unlikely to have any practical impact.

50. In terms of proposed text for the IFRS based FReM, John Thornton welcomed clarification on advances to the contingency fund and added that it would be useful to have all relevant guidance in one place. In addition, Ian Mackintosh suggested that the references to financing should be taken out of the definitions in the proposed interpretation.
51. However, several Board members (including Ken Wild and Robin Lynch) had concerns about the proposals, and Ken Wild in particular made the point that IAS 18 does not address profits, but addresses revenue. It was thought that the paper mixed up revenue, gains and losses. He also confirmed that revaluation does not fall into the definition of revenue.
52. Ian Carruthers suggested that the paper needed to consider the new IPSASB Standard on non-exchange revenues before proceeding. Scott Mackay was concerned that the proposals meant IAS 18 would be adopted, only for the requirements to be changed shortly afterwards.
53. Preliminary views on the new Standard are expected in January 2007 with the final version likely to be issued in 3-4 years time.
54. It was agreed that the Treasury would resubmit the paper to the Board having considered the new Standard. Ken Wild, Ian Carruthers and Robin Lynch were happy to be consulted on the revised paper before its submission to the Board. It was noted that the Treasury might have to consult further with departments.

Item 11: NHS Foundation Trusts Financial Reporting Manual 2006-07 (FRAB (83)11)

55. Miranda Carter presented this paper, which asked the Board to approve the list of divergences from the Government Financial Reporting Manual (FReM) in the 2006-07 Foundation Trusts Financial Reporting Manual (FT FReM). She highlighted the only new divergence, the treatment of Lottery Fund grants which will be treated as Government grants under SSAP 4 (rather than as donated assets). Robin Lynch felt that if money was being given by a public corporation then it should be treated as a donated asset. Anne Rylatt said that, if it was appropriate to treat Lottery grants as government grants in the FT FReM, it was also appropriate for the FReM. The Board agreed the divergence for the FT FReM and the Treasury would consider whether it was appropriate to be included in the FReM.

Item 12: IFRS 2: Share Based Payments (FRAB (83)12)

56. The Secretary presented this paper, which considered the application of IFRS 2: Share Based Payments in the IFRS based FReM. The Standard is similar to FRS 20: Share Based Payments and the Secretary recommended a similar approach, i.e. to note that the

Standard has no relevance to public sector accounting. David Heald queried whether it was possible that an entity which followed the FReM could have a subsidiary that made share based payments. It was agreed that the IFRS based FReM should make reference to IFRS 2 but should say that it was unlikely to apply in the public sector, but if it did, it should apply in full.

Item 13: IAS 33: Earnings per Share (FRAB (83)13)

57. The Secretary presented this paper, which considered the application of IAS 33: *Earnings per Share* in the IFRS based FReM. The Standard is similar to FRS 22: Earnings per Share which the FRAB had previously agreed was not relevant to the public sector and the Secretary recommended a similar approach, i.e. to note that the Standard has no relevance to public sector accounting. It was agreed that the Standard was generally not applicable but that the FReM should include reference to the Standard and say that while it generally won't apply, should it apply, then it will apply in full.

Item 14: IAS 34: Interim Financial Reporting (FRAB (83)14)

58. The Secretary presented this paper, which recommended that the IFRS based FReM should note that IAS 34: *Interim Financial Reporting* was unlikely to be relevant so to the public sector. Russell Frith cited one example where it would be, Scottish Water.

59. Ian Macintosh expressed his concern that the requirements of the Standard should be fully considered in any revised paper. The Board asked that the relevance of the Standard to the public sector be reconsidered and that a revised paper be resubmitted at the next FRAB meeting.

Item 15: Forward Work Programme (FRAB (83)15)

60. The forward agendas for the FRAB had been circulated. In response to the question of when the IFRS based FReM would be completed the Secretary highlighted that it was planned to complete the draft IFRS based FReM by the summer, and that the Board would have a second opportunity to look at the draft following final HMT consultation with departments.

61. David Heald reported to the Board that he had seen evidence of different treatment of impairments in the public sector and that it would be helpful if the Treasury, in submitting its IAS 36 Impairments of Assets paper, could include how impairments are currently accounted for in the FReM.

Any Other Business

62. The Secretary reported that Treasury officials are reconsidering the issue of capital charges in early January, and that following this meeting it is anticipated that the capital charging working group will

convene. It is anticipated that Treasury will report back to the Board at the February meeting, and no later than the March meeting.

Date of the Next Meeting

63. The Board confirmed the dates of the next meetings as:

Monday 12th February 2007

Monday 19th March 2007

Tuesday 24th April 2007