

SUMMARY REPORT

MEETING OF THE ACCOUNTING REGULATORY COMMITTEE OF 20 DECEMBER 2004

M. Wright, Director for Financial Markets, DG Internal Market chaired the thirteenth meeting of the Accounting Regulatory Committee.

1. VOTE ON A DRAFT REGULATION RELATED TO IFRS 2

Result of the vote on a Proposal for a Commission Regulation amending Regulation (EC) No 1725/2003 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council, as regards International Financial Reporting Standard (IFRS) No 2 with the consequential amendments to other previously endorsed IASs and IFRSs.

23 Member States (= 302 votes) voted in favour of the draft Commission Regulation proposing the endorsement of IFRS No 2 with the consequential amendments to other previously endorsed IASs and IFRSs. One Member State (=12 votes) abstained because of a reservation on the translation and another Member State (=7 votes) was not present.

2. POSITIONS OF THE MEMBER STATES CONCERNING THE PROPOSAL FOR A COMMISSION REGULATION

Some Member States suggested some amendments to the recitals (4-6) of the draft Commission Regulation. The suggested amendments were:

- Recital 4: Delete the fourth sentence of the recital and slightly redraft the beginning of the fifth sentence.
- Recital 5: Redraft the third sentence as follows: “The Commission recognizes that, in view of the potential impact, such as on employee stock option schemes, and the possible implications for the competitiveness of EU companies, the application should be regularly monitored.”
- Recital 6: The last sentence should be deleted.

The Commission accepted to make the necessary amendments to the text.

The Chairman pointed out the stable platform of all IASs/IFRSs and SICs/IFRICs in place as per 31 March 2004 were now endorsed.

3. OTHER AGENDA POINTS

Agenda item 1 – Approval of the agenda and the minutes of the ARC meeting of 30 November 2004

The minutes of the meeting were adopted after the comments from one Member State were taken on board.

Agenda item 3 – Information about the state of play on IAS 39 (full fair value option and interest rate margin hedge)

The Commission is carefully monitoring the debate by banking supervisors on the preliminary draft of a revised IAS 39. Recent developments are not encouraging.

In October 2004, Sir David Tweedie told the Commission that the IASB would take a decision in December 2004 on the full fair value option, which will not happen now. On 6 December 2004, the IASB issued a “preliminary first draft of a possible new approach” for the fair value option. Thereafter, “*one or more roundtable discussions*” during February or beginning of March should take place. So any IASB decision will be delayed until March 2005 at least.

However, the Basle Committee and the ECB are opposed to this recent IASB draft. A principles based approach seems acceptable, but robust principles are necessary according to the ECB/Basle Committee. The main reason is that the fair value option in the draft is too wide. For instance, no admission test requiring a “documented risk management strategy” for assets and liabilities being managed together on a fair value basis have been foreseen.

The debate will continue in January next year, when the IASB will evaluate all the comments received on the draft. The deadline for comment is 31.12.2004.

On the interest margin hedge, the IASB and the FBE are discussing various proposals advanced by the FBE. Although there is no agreement, the Commission understands that these discussions are proceeding in a positive climate and that there are hopes of arriving at a satisfactory solution. The next meeting between the representatives from the banking sector and the IASB has tentatively been scheduled for 17 January.

One Member State expressed its support for the IASB’s proposal on the fair value option and urged the Commission to achieve results on this issue as soon as possible.

Agenda item 4 – The Constitution Review of the IASCF

The Chairman said that there is a growing concern in political circles about the IASB's lack of democratic accountability and the way it is carrying out its work. In September 2004, the European Parliament sent a letter to the Commission requesting the Commission "*to suggest measures aimed at improving the governance of the International Accounting Standards Board*".

In a speech of 6 December 2004 given at a CESR conference Mrs. Berès, who chairs the European Parliament's Economic and Monetary Affairs Committee, mentioned IASB as an example of a potential loophole in democratic accountability, citing the delegation of power to a body under no democratic control.

On 23 November 2004, the Trustees of IASC Foundation published a consultation document containing their proposals to amend the IASC Foundation Constitution. The deadline for comments is 23 February 2005. The consultation document does not deal in detail with the funding of IASB but asked the Trustees "to satisfy themselves that appropriate financing arrangements are in place". The following issues were discussed:

- (a) That the IASB members should be closer to those who have to apply and to those who benefit from IASs, i.e. the business community and the investors from Europe and other environments where IASs are directly applicable. At present, only seven members come from countries where IASs are actually accepted and applied. This is too low. High quality people from different backgrounds should be on the Board of the IASB, not only accounting theoreticians.

First reactions from Member States

Two Member States felt that no geographical group should dominate but that also expertise is important.

- (b) The latest IASC consultation document suggests the majority needed for adopting a standard should increase to 9 out of 14 members, i.e. 64% of the Board members. But the Commission has argued for 10 members to vote in favour in order to provide sufficient safeguards that the standards are broadly acceptable. [Cf. A standard can only be endorsed

if it gets the support of 71% of the Member States in the Accounting Regulatory Committee].

First reactions from Member States

One Member State did not have strong views but was not opposed to the idea that 10 IASB members to be in favour for adoption of any standard, although it pointed out that this would make it easier for a small group to block progress.

(c) The professional qualifications required from candidates to the IASB; opening possibilities for persons with wider knowledge and more practical perspectives to be included on the Board.

First reactions from Member States

One Member State said that there should be a distribution between professional backgrounds of the candidates but also specific categories of professionals. Another Member State said that the greater flexibility regarding backgrounds in the current proposal was helpful, and would appear to cover all relevant backgrounds.

(d) Board Members should be able to communicate in an international environment. It should be part of the requirements for becoming a Board member.

First reactions from Member States

One Member State said that Board Members were already required to have communications skills and it couldn't see any need for additional wording.

(e) The IASB must have transparent and effective due processes, which are systematically employed to ensure that concerns of those who have to apply IASs are sufficiently taken into consideration. This should be laid down in a Charter of Due Process and it should be made mandatory.

First reactions from Member States

One Member State disagreed with the need to have a Charter of Due Process, as the IASB already planned to publish its operating procedures and principles. Another Member State stressed the importance of due process when ever decisions on International Financial Reporting Standards are taken.

(f) The oversight role and independence of the Trustees vis-à-vis the IASB is not strong enough. The Board of Trustees should be able to set and prioritise the IASB's work program. It should also be able to initiate the dismissal of the Chairman of the IASB. In addition, it is not fully satisfactory that the Trustees appoint other Trustees. No outside mechanism for the appointment of Trustees has been suggested.

First reactions from Member States

Two Member States were of the opinion that the Trustees should satisfy themselves that the work program is manageable and the appointment procedure is transparent and observable. The Trustees must also have influence on the Board.

(g) The Standard Advisory Council (SAC) has currently 50 members. Its number should be reduced significantly in order to become a pro-active forum, an independent and counterbalancing partner of the IASB. It should be a sounding board more than an assembly listening to IASB members explaining their work.

First reactions from Member States

One Member State agreed that the SAC should be a sounding board.

Many Member States made observations on the first outline to a response letter prepared by the Commission. Some Member States whilst agreeing with most of the main positions of the Commission's draft wanted a more balanced presentation stressing that the content of the response letter should be factual and should also concentrate on the existing problems with the international accounting standards e.g. the fair value option; service concessions etc. which are taking a long time to solve. The reasoning behind the comments should be given. One Member State put importance on the democratic legitimacy of the Board.

Member States were invited by the Commission to send in written comments on the Constitution Review of the IASCF after which the Commission will send a new draft response letter for comments to Member States.

The Chairman said that the funding of the IASB might be discussed at the next meeting.

Agenda item 5 – Service Concessions

The Chairman explained the reasons behind the need to have an interpretation for the Service Concessions.

Like any other industry, where no specific accounting treatment is required by the standards or interpretations, companies have to apply the hierarchy of norms as laid down in IAS 8 “*Accounting Policies, Changes in Accounting, Estimates and Errors*” from 1 January 2005.

At present, IASs/IFRSs do not contain any specific rules for service concession arrangements. For this reason, the IASB asked its interpretations committee, IFRIC, in April 2003 to examine whether a solution could be developed in the short time for service concessions.

IFRIC started the work in November 2003 and is still dealing with the issue. A draft interpretation would not be issued before the beginning of February 2005 and the final interpretation would not be known prior to July 2005 at the earliest. In any event, the final interpretation will not apply before 2006.

In order to speed up the process, the Commission asked EFRAG to contribute pro-actively to the IFRIC project.

In mid November 2004 EFRAG sent a letter to IFRIC, mainly dealing with some provisions of the future interpretation and the transition regime. No reply has been given from IFRIC to date.

Some Member States expressed their gratitude to EFRAG for the efforts made to solve the problems. Clearer guidance is needed on this issue.

The Chairman responded that it might be necessary for the Commission to send a letter to the IASB to point out the importance of having an interpretation in place as soon as possible.

Agenda item 6 – Date of Application of IFRSs and IFRICs after 2005

The Chairman explained that the date of application of a certain international accounting standard must be built on jurisprudence. Articles 4 and 9 of the IAS Regulation refer to the financial year when a certain international accounting standard adopted by the procedure laid down in Article 6(2) of the IAS Regulation shall be applied in the preparation of the consolidated accounts. Retrospective application of a standard is possible according to Judgement 368/89 of the European Court of Justice from 1991. According to this Judgement, retrospective application of law is forbidden except for cases where there are legitimate expectations to apply the law e.g. IFRIC 2 [Members’ Shares in Cooperative Entities and Similar Instruments]. After comments from some Member States it was decided that a

standard text formula for the date of application of a certain standard should be developed and be inserted in each draft for a Commission Regulation to have legal certainty. Following a request from one Member State the Commission will also set out its considerations in a working document.

Agenda item 7 – Impairment Test and the Accounting Directives

The Chairman recalled that at the last meeting one Member State asked whether non-amortisation of positive goodwill and treatment of negative goodwill under IASs/IFRSs is consistent with the Accounting Directives.

The Commission has circulated a working paper on this issue. The conclusion is that the non-amortisation of positive goodwill coupled with - at least - annual impairment reviews is consistent with the Accounting Directives and that no changes are required to permit the use of IASs/IFRSs.

The paper also concludes that the treatment of negative goodwill under IASs/IFRSs is not inconsistent with the Accounting Directives and that no changes are required to permit the use of IAS/IFRS.

Following a question from one Member State the Commission made clear that this reasoning in the working paper is relevant only to listed companies to the extent the IAS Regulation applies.

Agenda item 8 – Update on new IFRSs and IFRICs issued by the IASB

EFRAG made a presentation on the recently issued IFRSs and IFRICs as well as amendments to existing IASs and SICs. These accounting standards were:

- IFRS 6 Exploration for and Evaluation of Mineral Resources
- IFRIC 3 Emission Rights
- IFRIC 4 Determining whether an Arrangement Contains a Lease
- IFRIC 5 Decommissioning, Restoration and Environmental Rehabilitation Funds
- IFRIC amendment to SIC-12: Scope of SIC-12 Consolidation–Special Purpose Entities
- Amendments to IAS 39 (transition and initial recognition)
- Amendments to IAS 19 Employee Benefits

Concerning IFRIC 3, EFRAG underlined that there are major difficulties whether it is going to be acceptable for EFRAG to give a positive endorsement advice on this interpretation to the Commission.

Agenda item 9 – Work Plan of the ARC and the Contact Committee for 2005

The Chairman explained that the two accounting committees i.e. the Accounting Regulatory Committee (ARC) and the Contact Committee of the Accounting Directives would be merged from the beginning of 2005, effectively having where necessary the meetings of both committees on the same day. There would not be any amendments to the Accounting Directives because of this arrangement.

The work plan indicating the dates for meetings during 2005 was handed out. The planned meeting dates would be: 25.2, 8.4, 27.5, 8.7, 30.9, 28.10 and 2.12. 2005.*

Agenda item 10 – Miscellaneous

The Chairman announced that the next ARC meeting would take place on 25 February 2005.

The agenda would possibly be:

- Funding of the IASB
- Finalising the response letter to the Constitution Review of the IASCF
- Draft note on the distribution of profits under the fair value regime following the request of one Member State
- Translation arrangements of IFRSs/IASs
- Information about the state of play on IAS 39
- Update on Service Concessions

* Following a meeting on 12 January 2005, the following dates were rescheduled as follows:

- meeting on 8/04/2005 moved to 05/04/2005
- meeting on 27/05/2005 moved to 20/05/2005
- meeting on 30/09/2005 moved to 07/10/2005

ACCOUNTING REGULATORY COMMITTEE
Meeting of 20 December 2004

PARTICIPANTS' LIST

Austria

Justizministerium

Finanzministerium

Finanzmarktaufsicht

Belgium

Fod. Economie

Cyprus

Ministry of Finance

Czech

Ministry of Finance

Denmark

Danish Ministry of Economic and Business Affairs

- Danish Commerce and Companies Agency

- Danish FSA

Estonia

Permanent Representation to the EU

France

Conseil National de la Comptabilité (CNC)

Ministère de l'Economie, des Finances et de l'Industrie (Trésor)

SGCI/Premier Ministre

Finland

Permanent Representation to the EU

Germany

Permanent Representation to the EU

Greece

Ministry of Economy and Finance

Hungary

Permanent Representation to the EU

Ireland

**Institute of Chartered Accountants in Ireland
Department of Enterprise, Trade and Employment**

Italy

**CONSOB
ISVAP
Ministry of Economy and Finance
Banca d'Italia**

Latvia

Ministry of Finance

Lithuania

**Ministry of Finance
Accounting Institute**

Luxembourg

**Commission de Surveillance du Secteur Financier
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Malta

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Slovenian Institute of Auditors

Ministry of Finance

Spain

Banco de España

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Sweden

Ministry of Justice

United Kingdom

Department of Trade and Industry

OBSERVERS

Iceland

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European Institutions/Committees

European Central Bank (ECB)

Committee of European Banking Supervisors (CEBS)

Committee of European Securities Regulatory (CESR)

Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)

European Financial Reporting Advisory Group (EFRAG)

Commission

David Wright, Director of DG Markt

Jürgen Tiedje, Head of Unit "G5: Accounting & Auditing",

Mikael Lindroos, Secretary to the ARC/ G5

Thomas Scholz/G5

Arto Leppilähti/G5

Mike Thom/G5

Manuel Altemir/G5