IN BRIEF

Accounting for Uncertainty in Income Taxes, An Interpretation of FASB Statement No 109, recently published by the Financial Accounting Standards Board (FASB), clarifies when to recognise or derecognise a tax asset or liability and will affect all SEC registrants for periods starting after 15 December 2006. The FASB is seeking to introduce some consistency in dealing with the inevitable uncertainty over whether a tax liability exists at all and how to determine the likely amount if it does.

The first step is recognition. The enterprise must first determine whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position.

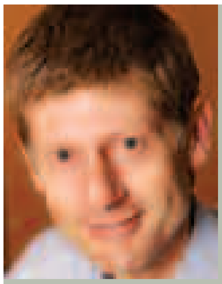
In evaluating whether a tax position has met the more-likely-than-not recognition threshold, the enterprise should presume that the position will be examined by the appropriate taxing authority that would have full knowledge of all relevant information.

The second step is measurement. A tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount to recognise in the financial statements. The tax position is measured at the largest amount that is greater than 50% likely of being realised on ultimate settlement.

Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognised in the first subsequent financial reporting period in which that threshold is met, and vice versa.

The European Commission is postponing the requirement for non-EU issuers to prepare their financial statements to international financial reporting standards (IFRS) or an "equivalent" GAAP until periods starting on or after 1 January 2009 – and likewise for the obligation to restate historical financial information included in a prospectus filed with a competent authority before 1 January 2009.

HM Treasury is consulting on the current form of the payment services directive. After going through the European Parliament, the directive has accrued some 639 amendments, many of which can be welcomed as making the new payment processes more practical and workable. The ACT will be feeding in the users' views. For more information contact **modonovan@treasurers.org.**



INTRODUCTION

By Martin O'Donovan
ACT Technical Officer

It is a real skill knowing when to home in on detail and when it is better to take the wider view. The successful manager can do either, as and when required. With legal agreements, getting the overall shape sorted is one thing but attention to detail will avoid countless pitfalls. So too with accounting. The news that the International Accounting Standards Board is going back to the basics and reviewing the framework for the preparation and presentation of financial statements sounds like motherhood and apple pie, but a subtle nuance at the fundamental level can have huge subsequent ramifications on the whole purpose of the accounts as the story opposite explains. ■

Market management exercises

Certain market management activities may appear dubious and potentially abusive practices banned by the Financial Services Authority (see *Box 1*). However, stabilisation or the buying back of recently issued securities for the purposes of supporting the price is permitted for a period after a new issue. If this is to occur, it must be disclosed before the opening of the offer period along with details of the parameters the manager is to work under.

Recently the FSA has been receiving queries about another market management practice, but this time it concerns the shorting of a reference bond, normally a gilt, ahead of the pricing of a deal. The short is then used in order to reduce the volatility of the reference bond as investors switch from the gilt into the new bond issue upon pricing.

The stabilisation rules and related disclosures apply to the new securities being issued and therefore the FSA has felt it necessary to comment in its June Marketwatch newsletter. The FSA thinks that issuers and their agents have three basic options if they are dealing in the reference bond:

(i) Full disclosure including terms, time frame, parties involved, prices, and so on;
(ii) Partial disclosure similar to details required of article 9 (1) (a) of the stabilisation regulation, stating that such activity may take place, perhaps including some of the parameters; or
(iii) No disclosure.

With full disclosure there is less risk of the activity being considered abusive but there is a chance of other market participants trading against the issuer's interests. Most participants, it appears, opt for partial disclosure.

Issuers of bonds who are subject to the listing rules and disclosure rules ought to consider if any of these arrangements constitute inside information. If an issuer concludes that the arrangements constitute inside information, then it should announce the details over a regulatory information service. ■

Box 1. FSA Code of Market Conduct 1.6

The Financial Services and Markets Act 2000 section 118 (Market Abuse) prohibits effecting transactions or orders to trade (otherwise than for legitimate reasons and in conformity with accepted market practices) which (a) give, or are likely to give, a false or misleading impression as to the supply of, or demand for, or as to the price of, one or more qualifying investments; or (b) secure the price of one or more such investments at an abnormal or artificial level.

Practical pension guidance

New codes of practice from the Pensions Regulator covering internal controls and member-nominated trustees and directors have been laid before parliament to become effective shortly. Although not statements of law, both codes offer practical guidance on the requirements of the Occupational Pension Schemes (Internal Controls) Regulations 2005 and the Pensions Act 2004.

Internal controls must be sufficient to

Death knell sounds for stewardship?

Another step on the road to the convergence of accounting standards has been taken by the IASB and the Financial Accounting Standards Board (FASB) in the US with the issue of a discussion paper setting out their preliminary views on the objective of financial reporting and the qualities that make the information useful for decision-making. This represents the first stage of a project to develop a joint conceptual framework that both standards boards will adopt to replace their separate frameworks.

It may be tempting to view such deliberations as nothing more than an irrelevant distraction, but they have far-reaching implications for the future direction of financial reporting, such as the debate on use of fair values, and challenge some of the fundamental concepts with which many finance professionals (especially in the UK) will be familiar.

Most importantly, the paper states: "The objective of general purpose external financial reporting is to provide information that is useful to present and potential investors and creditors and others in making investment, credit, and similar resource allocation decisions."

The absence of any reference to "stewardship" is noticeable. The paper argues that the concept of stewardship is retained since those interested in assessing it are generally interested in making resource allocation decisions, but this is causing some disquiet among investors who value information on management performance.

This view was supported by two IASB board members (both British, including Sir David Tweedie), who preferred stewardship to be identified as a separate objective of financial reporting, arguing that while stewardship and decision-usefulness do not necessarily conflict, they do have different emphases. These sentiments were outvoted 12-2 in the IASB vote, but such concerns are clearly not shared in the US where the paper was carried unanimously by the FASB, perhaps fuelling concerns that achieving convergence will require others to move towards the US view.

The boards' proposals designate as the primary users of financial reports a broader group than existing ordinary shareholders, including potential investors and present and potential creditors. While their expectation is that the needs of these other groups will essentially be the same as the needs of existing shareholders, they believe that designating only ordinary shareholders as the primary users could imply an inadequate focus on creditors' needs (for example, with respect to disclosures).

As with some of the European transparency directive requirements creeping into UK company law, changes of this sort raise questions on whether the company will become legally liable to a wider group of interested parties.

The second part of the paper proposed a number of qualitative characteristics of decision-useful financial reporting information: relevance, comparability and understandability, all of which are subject to two constraints – materiality and benefits that justify costs.

The category of reliability is to be replaced by "faithful representation" but in making this apparently slight change the concept of substance over form, which was a component of reliability, has been omitted. It is still deemed important on the basis that it is implied in the concept of faithful representation, but in that case why not include mention of it?

The discussion raised another concept close to the hearts of many finance professionals, that of "true and fair view". The boards concluded that this was not a qualitative characteristic but should result from applying the qualitative characteristics, and that it was much the same as "faithfully represent", which is one of the proposed characteristics.

Comments on the exposure draft must be submitted by 3 November 2006. The ACT will be submitting a response and if you wish your views to be considered during the drafting of this, please contact a member of the technical team. ■

IN BRIEF

▸ The **IAS37 *Contingent Liabilities* redeliberations** are continuing at the IASB. Recent board meetings seem determined to remove the previous probability recognition criterion whereby contingencies are not recognised until they become "more likely than not" in favour of a liability definition to drive recognition and then apply probabilities to the measurement. The ACT has previously submitted its view that recognition of remotely probable liabilities, even at a reduced amount, is not helpful in terms of reliability of information and its faithful representation (see *The Treasurer*, October 2005, p48). It is also strangely at odds with the moves by the FASB on taxation mentioned opposite.

▸ **The IASB has announced a period of stability on international financial reporting standards (IFRS).** No new standards will be required to be implemented before 1 January 2009, although voluntary early adoption will be permitted. As a general rule the intention is to allow at least a year between publication and required implementation of new standards. There is also to be more opportunity for input on conceptual issues arising out of the joint IASB/FASB work programme by means of discussion papers rather than moving straight to exposure drafts.

▸ **An amended version of the Combined Code** was published by the Financial Reporting Council (FRC) at the end of June 2006, substantially as proposed in January. The slight variations are that the inclusion of a vote withheld category on proxy forms will apply to all general meetings, not just AGMs, and that the obligation to publish the results of voting on the web can be via a site maintained on behalf of the company and not solely the official company website. The FRC encourages adoption of the updated code on a voluntary basis for reporting years beginning on or after 1 November 2006, although the listing rules will not apply to the revised Combined Code until a separate consultation has been carried out by the UKLA.

ensure that the scheme is administered and managed in accordance with the scheme rules and the relevant legislation. The code provides guidelines on developing a risk management framework, helping trustees to focus on the key risks to their schemes.

The second of the codes covers advice on how trustees should ensure arrangements are in place, and implemented, for at least one third of trustees to be member-nominated; or at least one third of directors of the trustee company to be member-nominated. The arrangements must include a nomination process, a selection process and other statutory requirements.