Financial Reporting Council

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Dear Jean-Paul

This letter sets out the comments of the UK Financial Reporting Council (FRC) on EFRAG's draft comment letter (DCL) to the IASB Exposure Draft (ED) ED/2018/1 '*Accounting Policy Changes (Proposed amendments to IAS 8)*'. Our detailed comments on EFRAG's DCL are set out in the appendix to this letter and we have included our response to the IASB for your information.

We broadly agree with EFRAG's DCL. Like EFRAG's DCL, our letter to the IASB highlights that the ambiguity regarding the status of agenda decisions published by the IFRS Interpretations Committee (IFRS IC) in relation to other non-authoritative literature, and the tension in distinguishing a voluntary change in accounting policy from the correction of an error, are likely to be exacerbated if the amendments are published as drafted in the ED. We suggest that the IASB clarifies the criteria for distinguishing a voluntary change in accounting policy from an error, irrespective of the amendments proposed in the ED.

We share EFRAG's concerns regarding the practicality of differentiating voluntary changes in accounting policy that result from an agenda decision from other voluntary changes in accounting policy. Therefore, it may not be clear if the proposed relief is available in a specific situation. Like EFRAG, we believe that all voluntary changes in accounting policy that result in reliable and more relevant information in financial statements should be encouraged, to improve the overall quality of reporting. Our letter to the IASB therefore suggests that the proposed relief from retrospective application is made available for all voluntary changes in accounting policy that are permitted by paragraph 14(b) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* (IAS 8). This would be more consistent with how the IASB sets requirements for changes in accounting policy that are required per paragraph 14(a) of IAS 8, as a result of new IFRSs or amendments to existing IFRSs; transition provisions often provide relief from retrospective application on cost/benefit grounds.

We also believe that practical guidance to assist companies with performing the cost/benefit analysis will be needed to ensure that it is applied in a consistent and sufficiently robust manner. We suggest that this is modelled on the step by step guidance in *IFRS Practice Statement 2 (Making Materiality Judgements)* and includes illustrative examples.

We support the IASB's decision not to mandate an effective date for voluntary changes in accounting policy that result from agenda decisions. In our view, a mandatory effective date would indicate that the change is required and therefore constitutes the correction of an error. We agree with EFRAG that the timeliness of the implementation of voluntary changes in accounting policy that result from agenda decisions may be better addressed through improved communication of agenda decisions to constituents.

If you would like to discuss these comments, please contact me or Rosalind Szentpéteri on 020 7492 2474.

Yours sincerely

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Appendix 1

Question 1

The IASB proposes to amend IAS 8 to introduce a new threshold for voluntary changes in accounting policy that result from an agenda decision published by the IFRS Interpretations Committee. The proposed threshold would include consideration of the expected benefits to users of financial statements from applying the new accounting policy retrospectively and the cost to the entity of determining the effects of retrospective application.

Do you agree with the proposed amendment? Why or why not? If not, is there any particular aspect of the proposed amendments you do or do not agree with? Please also explain any alternatives you would propose, and why.

The status of agenda decisions and distinguishing changes in accounting policies from errors

We agree with EFRAG's observation that the proposed amendments may cause confusion regarding the status and objectives of agenda decisions in comparison to the "other accounting literature" referred to in paragraph 12 of IAS 8. We share EFRAG's concern that introducing separate requirements for voluntary changes in accounting policy that result from agenda decisions could be interpreted as elevating the status of agenda decisions above the status of other forms of non-authoritative literature and is likely to exacerbate the difficulties that can arise in distinguishing a voluntary change in accounting policy from the correction of an error. Our letter to the IASB highlights this tension and states that the IASB should clarify the circumstances in which a change in accounting policy constitutes a voluntary improvement or the correction of an error, irrespective of the amendments proposed in the ED.

Relief from retrospective application

We do not support the IASB's proposal to apply different requirements to voluntary changes in accounting policy that result from agenda decisions published by the IFRS IC and other voluntary changes in accounting policy. We do not believe that the proposals as drafted are practicable because it is not clear on what basis a company should determine whether a voluntary change in accounting policy "results from an agenda decision". As noted in EFRAG's DCL, a company's accounting policies may be similar but not identical to the facts and circumstances described in the agenda decision and this may lead to confusion about whether the proposed relief is available in a specific case, resulting in diversity in application.

In our view, voluntary changes in accounting policy that result in reliable and more relevant information in the financial statements—and are therefore permitted by paragraph 14(b) of IAS 8—should be encouraged, to improve the quality of information available to investors. Like EFRAG, we believe that retrospective application is equally likely to be a hindrance to implementing voluntary changes in accounting policy regardless of whether those changes result from an agenda decision. Therefore, we agree with EFRAG that it would be preferable

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for the IASB to make the proposed relief from retrospective application available for all voluntary changes in accounting policy that meet the requirements of paragraph 14(b). Limiting the retrospective application of any voluntary change in accounting policy to those cases where the benefits to the primary users exceed the costs to preparers appears reasonable to us. In our view, the impracticability threshold for voluntary changes in accounting policy is unduly burdensome.

Proportionate relief from retrospective application should be viewed as a practical expedient to encourage beneficial improvements to reporting, consistent with the IASB's approach to retrospective application for changes in accounting policy that are required per paragraph 14(a) of IAS 8, as a result of new IFRSs or amendments to existing IFRSs. The IASB often provides such relief on the basis of its analysis of costs/benefits, for example through transition provisions allowing a modified retrospective approach. In our view, the same underlying cost/benefit principles should be applied to both required and voluntary changes in accounting policy, the only difference being that for voluntary changes the cost/benefit analysis would need to be performed by the company rather than the IASB.

Analysis of costs versus benefits

We agree with EFRAG that the description in paragraphs A6-A10 of the ED of factors to consider when performing the cost/benefit analysis is too generic. Our letter to the IASB suggests that it is supplemented with practical guidance that illustrates the steps of the process that companies should apply to determine the extent of retrospective application required. Smaller companies, in particular, are likely to need guidance on how to weigh the costs against the benefits, particularly as the benefits may not be simple to quantify. Step-by-step guidance could be structured similarly to the process for making materiality judgements set out in *IFRS Practice Statement 2* (*Making Materiality Judgements)*. In the absence of such practical guidance we believe that the cost/benefit analysis may not be performed in a consistent and sufficiently robust manner. We believe that illustrative examples would also be helpful.

Question 2

The IASB decided not to amend IAS 8 to address the timing of applying a change in accounting policy that results from an agenda decision published by the IFRS Interpretations Committee. Paragraph BC18-BC22 of the Basis for Conclusions on the proposed amendments set out the IASB's considerations in this respect.

Do you think the explanation provided in paragraphs BC18-BC22 will help an entity apply a change in accounting policy that results from an agenda decision? Why or why not? If not, what do you propose, and why? Would you propose either of the alternatives considered by the IASB as outlined in paragraph BC20? Why or why not?

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Effective date for a voluntary change in accounting policy resulting from an agenda decision

Like EFRAG we support the IASB's decision not to mandate an effective date for voluntary changes in accounting policy resulting from agenda decisions. We agree with the reasoning in paragraph BC22 of the ED and we do not believe that either of the alternatives suggested in paragraph BC20 would be operable.

Our letter to the IASB also notes that the difficulties arising from the ambiguity around the status of agenda decisions are relevant to the discussion of effective dates. Mandating an effective date would indicate that the company is required to change its accounting policy to comply with IFRS and that the change in accounting policy therefore constitutes the correction of an error identified upon publication of the agenda decision, rather than a voluntary change in accounting policy.

We agree with EFRAG's suggestion that the timeliness of the implementation of voluntary changes in accounting policy resulting from an agenda decision may be addressed more effectively through improved communication of agenda decisions to constituents. However, we do not support the suggestion in paragraph 33 of EFRAG's DCL that the IASB consider limiting the benefit of the lower threshold for a certain period of time. In our view, this may undermine the aims of the proposed amendments (i.e. to remove a barrier to improving the quality of reporting and consistency in the application of IFRS).

Transition provisions for the proposals in the ED

Like EFRAG, we disagree with paragraph BC14 of the ED which states that "there is no reason to either allow or require an entity to change its accounting for changes in accounting policy made before that date." As noted above, we do not believe that the Board can require voluntary changes in accounting policy. However, we see no reason why the Board would not make the relief from retrospective application for voluntary changes in accounting policy available to companies immediately upon publication of the changes to IAS 8, to facilitate earlier implementation of voluntary changes that would improve the relevance of the information in companies' financial statements.

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