



**The Hundred Group**  
of Finance Directors

## **Financial Reporting Committee**

Michelle Sansom  
Technical Director  
Accounting Standards Board  
5<sup>th</sup> Floor, Aldwych House  
71-91 Aldwych  
London  
WC2B 4HN

21 May 2012

Dear Michelle

### **Revised Financial Reporting Exposure Drafts: The Future of Financial Reporting in the UK and Republic of Ireland**

We are pleased to submit our comments on the following revised exposure drafts: FRED 46 (Draft FRS 100) 'Application of Financial Reporting Requirements'; FRED 47 (Draft FRS 101) 'Reduced Disclosure Framework'; and FRED 48 (Draft FRS 102) 'The Financial Reporting Standard'.

#### **Who we are**

The Hundred Group is a non-political, not-for-profit organisation which represents the finance directors of the UK's largest companies, with membership drawn mainly, but not entirely, from the constituents of the UK FTSE100 Index. Our aim is to contribute positively to the development of UK and international policy and practice on matters that affect our businesses, including taxation, pensions, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the views of The Hundred Group of Finance Directors as a whole, they are not necessarily those of our individual Members or their respective employers.

#### **Scope of our comments**

Our members are listed companies that are required to prepare their consolidated financial statements in accordance with EU adopted IFRS. It is therefore likely that most of our members will adopt EU adopted IFRS in their separate financial statements and in the financial statements of their UK subsidiaries and, where permitted to do so, will take advantage of the reduced disclosures permitted by FRS 101. We have therefore focused our comments on the overall objectives of the Board's proposals contained within FRED 46 and FRED 47.

We will leave it to others with greater resources than ourselves to comment on the detailed application of FRED 48.

Our responses to the specific questions asked by the Board are set out in the Appendix.

#### **We welcome the Board's revised proposals**

We continue to support the Board in its efforts to replace existing UK GAAP with a financial reporting framework that provides high quality and understandable financial statements

information that are proportionate to the size and complexity of the entities concerned and the needs of users.

We commend the Board for its willingness to reconsider its initial proposals and for the considerable effort that it has put into its outreach activities.

We support the financial reporting framework outlined in draft FRS 100. We are pleased that Board does not seek to impose IFRS on UK companies but would permit them to adopt either EU-adopted IFRS or standards based on IFRS for SMEs.

We were one of the representative groups that first mooted the idea of reduced disclosures for UK subsidiaries. We are pleased to see that the Board now proposes the extension of reduced disclosures in draft FRS 101 and draft FRS 102 to all 'qualifying entities'.

We consider that FRS 102 will improve UK GAAP, in particular by introducing requirements on accounting for financial instruments, and will do so in a way that will be proportionate to the needs of users. We expect that once the transition phase has been overcome, FRS 102 will have the effect of reducing the reporting burden on those UK companies that adopt it compared with existing UK accounting standards. We remain concerned, however, about the effect and practicability of the proposals with regard to accounting for multi-employer pension schemes.

While we expect the new reporting framework to be beneficial in the long run, the new standards are rather more complex than we hoped they would be. We expect that many companies will require considerable assistance from their advisers in implementing the new standards. We would warn the Board to expect some adverse comment from its constituents for imposing short term pain at a time when UK industry could well do without it.

### **Compliance with company law**

We understand that the benefits of the proposed framework are unlikely to be capable of realisation without changes to the Companies Act 2006 and the EU's 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives. While changes are proposed to the EU's Directives that may resolve some of the conflicts we recognise that some of the conflicts will remain. We urge the Board to work together with BIS in an attempt to resolve these conflicts.

We believe that it will be difficult for entities that adopt FRS 101 to comply with both IAS 1 *Presentation of Financial Statements* and the formats for the profit and loss account and the balance sheet prescribed by the Companies Act 2006 and related regulations. For the avoidance of confusion and unnecessary complexity, we recommend that the Board requires entities that adopt FRS 101 to comply only with company law in this respect and not also with IAS 1.

We note that the Board has already proposed that entities that adopt FRS 102 should comply with the company law formats and not those contained in IFRS for SMEs.

### **Reduced disclosures for qualifying entities**

#### Equivalent disclosures

An entity may take advantage of the disclosure exemptions set out in paragraph 8 of FRED 47 only if equivalent disclosures are provided in the consolidated financial statements of its parent entity. Paragraph 9 of FRED 47 cross refers to the Application Guidance to draft FRS 100 in deciding whether the consolidated financial statements of the parent provide equivalent disclosures.

We request that the Board clarifies how the equivalence criteria apply in situations where items are reflected in the financial statements of a parent or a subsidiary that are eliminated on consolidation, i.e. would the parent or subsidiary be denied a disclosure exemption in relation to an item that is not reflected in consolidated financial statements and for which there are therefore no equivalent disclosures.

We suggest that instead of requiring specific disclosures to be included in the consolidated financial statements of the parent entity, FRED 47 simply requires that the subsidiary is included in consolidated financial statements of the parent entity that have are prepared in accordance with IFRS as adopted for use in the EU or accounting standards that are considered to be equivalent within the meaning of the EU's Seventh Directive.

#### Reference to disclosure exemptions

Paragraph 7(c) of FRED 47 requires a company to list the relevant standard and paragraph references of the disclosure exemptions it has adopted. We do not consider that this would be meaningful for the users of the financial statements. We therefore suggest that the company should instead be required to describe the nature of the disclosure exemptions that it has adopted.

#### Approval process

While paragraph 7(a) of FRED 47 prescribes the shareholder approval required by entities that wish to take advantage of reduced disclosures, it does not provide any guidance on the process which must be followed in obtaining such approval, e.g. it does not expand on how and in what time period a shareholder may object. We suggest that the Board agrees with BIS whether such guidance should be provided in accounting standards or in company law. Whichever medium is decided upon, we suggest that the approval process should be consistent with that which an entity must follow under company law if it wishes to relieve itself of the obligation to prepare consolidated financial statements.

#### **Multi-employer pension schemes**

We are concerned that the proposed reporting framework does not feature the exemptions from accounting for multi-employer pension schemes as defined benefit schemes that are currently provided by FRS 17 *Retirement benefits*. We believe that not only will this create practical difficulties because it will be necessary somehow to apportion scheme assets and liabilities but also it could cause dividend blocks where the recognition of a pension deficit reduces distributable profits.

We expect that this will be a particular issue for parent entities and their subsidiaries that participate in group pension schemes.

We sense little or no progress towards reform of the UK law in relation to distributable profits and therefore urge the Board to revisit the proposed accounting for multi-employer pension schemes. We recognise that this would entail an amendment to EU adopted IFRS for use in the UK as well as draft FRS 102.

#### **Implementation timetable**

We agree with the proposed mandatory implementation for periods beginning on or after 1 January 2015. Assuming the new standards are published by the end of 2012, this will allow plenty of time for companies to effect the transition. We are concerned, however, that any further slippage on the part of the IASB in relation to its revised standards on financial instruments, revenue recognition and leases may necessitate the deferral of the effective date of FRS 102.

We expect that many of our members may wish to transition to EU adopted IFRS with reduced disclosures as soon as possible in order to achieve consistency with group reporting requirements. We therefore suggest that if there should be a significant delay in finalising FRS 102, the Board should proceed with issuing FRS 101.

### **Due process**

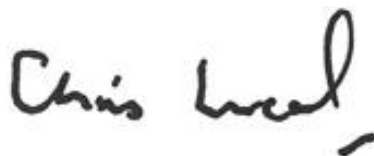
We are surprised by the extent to which FRS 102 diverges from IFRS for SMEs. While this may be necessary to comply with company law and to make the standard suitable for use in the UK, there is no doubt that the extent of the divergence means that the Board will have an important role to play in maintaining FRS 102.

As companies and their advisers start to address the practical implications of implementing FRS 102, it is likely that issues requiring clarification or interpretation will be identified. We anticipate that there will be a considerable number of these issues due to the limited application guidance contained in FRS 102 and the lack of experience in the UK of applying IFRS for SMEs which provides the basis for FRS 102. We recommend that the Board clarifies the due process that it will follow in relation to requests for clarification and interpretation.

We are mindful that FRS 102 will need to be reviewed in the light of changes to EU adopted IFRS and IFRS for SMEs. We recommend that the Board issues supplementary exposure drafts prior to the finalisation of FRS 102 to reflect not only IFRS 9 Financial Instruments but also the IASB's revised standards on revenue recognition and leases. We believe that there should be a stable platform for UK companies both at least 18 months before the mandatory adoption of FRS 102 and for a reasonable period after adoption. We consider it important that the Board makes clear to its constituents the process for and the likely timing of updates to FRS 102.

Finally, we would like to wish the Board well in finalising the new standards. Please feel free to contact me if you wish to discuss our comments.

Yours sincerely

A handwritten signature in black ink that reads "Chris Lucas". The signature is written in a cursive, slightly slanted style.

**Chris Lucas**  
*Chairman*  
*The Hundred Group - Financial Reporting Committee*

## **QUESTION 1**

The ASB is setting out the proposals in this revised FRED following a prolonged period of consultation. The ASB considers that the proposals in FREDs 46 to FRED 48 achieve its project objective:

**To enable users of accounts to receive high-quality, understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.**

**Do you agree?**

Given that the Board decided to cease the independent development of UK GAAP some years ago and has since been focused on alignment with IFRS, we believe that there is now no realistic alternative for the UK other than to adopt accounting standards based upon IFRS for SMEs. We believe that, in the circumstances, the Board's proposals represent a practical solution for the future of financial reporting in the UK.

We are pleased that the proposals would not impose IFRS on UK business but would permit companies to adopt either EU-adopted IFRS or standards based on IFRS for SMEs with reduced disclosures in certain circumstances. We therefore believe that the proposals would result in financial reporting that is proportionate to the size and complexity of entities and the information needs of users of their financial statements.

## **QUESTION 2**

**The ASB has decided to seek views on whether:**

**As proposed in FRED 47**

**A qualifying entity that is a financial institution should not be exempt from any of the disclosure requirements in either IFRS 7 or IFRS 13; or**

**Alternatively**

**A qualifying entity that is a financial institution should be exempt in its individual accounts from all of IFRS 7 except for paragraphs 6, 7, 9(b), 16, 27A, 31, 33, 36, 37, 38, 39, 40 and 41 and from paragraphs 92-99 of IFRS 13 (all disclosure requirements except the disclosure objectives).**

**Which alternative do you prefer and why?**

Over the years, we have criticised the IASB for imposing upon entities that are not financial institutions disclosures that are principally intended to portray the activities of financial institutions. We have also criticised the IASB for cluttering financial statements with unnecessary disclosures.

We therefore support the exemptions that are contained in FRED 47 (FRS 101) for qualifying entities that are not financial institutions in relation to the disclosure requirements of IFRS 7 and IFRS 13. We agree that financial institutions should not qualify for exemption from IFRS 7 or from any disclosures contained in IFRS 13 in so far as they relate to financial instruments. While this approach may be considered to be draconian by some financial institutions, they should bear in mind that no disclosure will be required in relation to items that are not material to their financial statements.

While we support full disclosure by financial institutions in relation to financial instruments, we do not see why they should be treated differently from other businesses in relation to other assets and liabilities. As FRED 47 is currently worded, financial institutions would be prohibited from taking *any* exemption from the disclosure requirements of IFRS13. We believe that qualifying financial institutions should be exempt from the disclosure requirements of IFRS 13 *except* in relation to financial instruments.

### **QUESTION 3**

**Do you agree with the proposed scope for the areas cross-referenced to EU adopted IFRS as set out in section 1 of FRED 48? If not, please state what changes you prefer and why.**

We recognise the need for FRED 48 to contain cross references to elements of EU adopted IFRS that are relevant to entities that have public accountability (because IFRS for SMEs, on which FRED 48 is based, is not designed for use by entities with public accountability that therefore contains no equivalent of such accounting standards). We therefore broadly agree with the proposed cross references to IAS 33 *Earnings per Share*, IAS 34 *Interim Financial Reporting* and IFRS 8 *Operating Segments* (for entities with, or in the process of issuing, publicly traded securities) and IFRS 4 *Insurance Contracts*.

We are mindful, however, that the form and content of interim financial reports has historically been prescribed by the body governing the market on which the securities are traded. We therefore suggest that the Board may wish to revisit the wording of the cross reference to IAS 34 to ensure that there would be no entities that will adopt FRS 102 that would thereby be required to comply with IAS 34 even though they are not required to do so by the relevant governing body, e.g. entities with securities publicly traded on the PLUS Stock Exchange in London.

### **QUESTION 4**

**Do you agree with the definition of a financial institution? If not, please provide your reasons and suggest how the definition might be improved.**

We understand that the implication of being a financial institution is: (a) for entities applying FRS 101, there is no exemption from the disclosure requirements of IFRS 7 and IFRS13; and (b) for entities applying FRS 102, there is no exemption from the disclosures required by Section 11 and 12 and there are additional disclosures required by Section 34. Apparently, the Board's intention is that a financial institution shall have no exemption from the applicable disclosures in relation to financial instruments.

We note that the Board has not identified a principle in determining the types of entities that are defined as financial institutions in FRED 46 (FRS 100). We recommend that the Board revisits the definition and considers, for example, whether all stockbrokers and insurance brokers should fall within the definition of a financial institution or only those that hold and manage client assets.

We do not believe that retirement benefit plans should be included within the definition of a financial institution. As we indicate in our answer to Question 6, we believe that the form and content of the financial statements of retirement benefit plans should continue to be dealt with by a SORP. Moreover, we believe that the disclosures that are required of a financial institution that are not reflected in the existing SORP are not relevant to the users of the financial statements of retirement benefit plans.

## **QUESTION 5**

**In relation to the proposals for specialist activities, the ASB would welcome views on:**

- (a) Whether and, if so, why the proposals for agriculture activities are considered unduly arduous? What alternatives should be proposed?**

We are concerned that the Board is seeking to impose on the UK's agricultural sector fair value accounting for biological assets. While this approach is consistent with EU adopted IFRS, the Board will appreciate that the appropriateness of this aspect of IAS 41 *Agriculture* has been questioned by many of the IASB's international constituents. Consequently, reform of IAS 41 is likely to feature on the IASB's three-year agenda that is due to be published soon.

Moreover, we understand that transition to fair value accounting is likely to be costly for producers and that many commentators question its relevance in the context of agricultural businesses.

We therefore urge the Board to amend IFRS for SMEs so as to permit agricultural businesses to measure biological assets on a cost basis until such time as the IASB has completed its review of IAS 41. We would encourage the Board to engender debate among its constituents in the agricultural sector with a view to contributing to the IASB's deliberations.

- (b) Whether the proposals for service concession arrangements are sufficient to meet the needs of preparers?**

We recognise that the proposals on service concession arrangements are copied directly from Section 34 of IFRS for SMEs.

We suspect that entities applying IFRS for SMEs to service concession arrangements will have referred to the more detailed guidance contained in IFRIC 12 even though it is not directly referenced from IFRS for SMEs.

While we expect that in the absence of further guidance preparers applying FRS 102 will similarly refer to IFRIC 12, we believe that FRS 102 should as far as is practicable be a stand-alone set of accounting standards. We therefore believe that additional guidance on accounting for service concession arrangements should be included within FRS 102.

## **QUESTION 6**

**The ASB is requesting comment on the proposals for the financial statements of retirement benefit plans, including:**

- (a) Do you consider that the proposals provide sufficient guidance?**
- (b) Do you agree with the proposed disclosures about the liability to pay pension benefits?**

We understand that the Board has decided that the SORP *Financial Reports of Pension Schemes* is to be updated to provide guidance on FRS 102 supplementing that set out in Section 34. We support the review of the pensions SORP but are concerned that the Board appears in FRED 48 to have unilaterally proposed changes to the reporting practice established by the pensions SORP. We would remind the Board that the SORP has been developed over many years based on the wide-cross section of pensions expertise

represented by the Pension Research Accountants Group and is tailored to address pension issues that are specific to the UK.

We are concerned that many of the disclosures that would be required to be presented in the financial statements would duplicate information that is presented elsewhere in the annual report of a retirement benefit plan.

We are not convinced that it is appropriate to disclose the obligation to pay future benefits in the financial statements of a retirement benefit plan. After all, the obligation is pointedly excluded from net assets statement by the pensions SORP. For the members of a pension plan, the willingness and ability of the sponsoring employer to fund any deficit existing on the plan is more important than the deficit at a point in time. Consequently, the information contained in the Summary Funding Statement is likely to be more relevant to members and to the Pensions Regulator where the assessment of the surplus or deficit on the plan is supported by extensive disclosure of the underlying assumptions. Moreover, if the benefit obligation were to be disclosed in the financial statements, audit fees would increase significantly for little or no benefit given that the benefit obligation is calculated by a qualified actuary subject to established professional standards.

We would welcome a review of reporting by retirement benefit plans but we believe that this should be by way of a comprehensive review of the pensions SORP in order that the annual report of a retirement benefit plan may be considered as a whole rather than on a piecemeal basis.

#### **QUESTION 7**

**Do you consider that the related party disclosure requirements in section 33 of FRED 48 are sufficient to meet the needs of preparers and users?**

We welcome the carry-over from FRS 8 *Related party disclosures* of the exemption from disclosure of transactions involving wholly-owned subsidiaries. However, we suggest that the Board adopts the relevant wording from the Companies Act rather than FRS 8 to avoid unnecessary inconsistencies.

We suggest that the Board clarifies the application of materiality in the context of related party transactions. In our opinion, a related party transaction should be disclosed in an entity's financial statements only if it is material to the entity, i.e. that the entity's financial position or profit or loss may have been materially affected by the transaction.

We are mindful of the potential inconsistencies between the disclosures required by IFRS for SMEs and those required by the Companies Act in relation to management compensation and transactions with management (including director's loans). We recommend that for application by UK companies the Board should amend the related party disclosure requirements of IFRS for SMEs in these respects to make them consistent with the Companies Act. In particular, we recommend that the Board ensures that the amounts to be disclosed by way of compensation of key management personnel are prepared on a basis consistent with the disclosures of directors' emoluments required by the Companies Act in order to avoid confusion.



## **QUESTION 8**

**Do you agree with the effective date? If not, what alternative date would you prefer and why?**

We agree with the proposed mandatory implementation for periods beginning on or after 1 January 2015. Assuming the new standards are published by the end of 2012, this will allow plenty of time for companies to effect the transition.

We are concerned, however, that there may be further slippage in the finalisation and effective date of IFRS 9 *Financial Instruments*. We understand that the Board intends to issue a supplementary exposure draft upon the finalisation of IFRS 9 with a view to updating Sections 11 and 12 of FRS 102. We assume that the Board will not wait until any consequential amendments have been made to IFRS for SMEs. While this may ensure sufficient time for companies to effect the transition, we are concerned that this approach may give rise to unintended differences between FRS 102 and IFRS for SMEs.

We are unclear how the Board will approach the alignment of FRS 102 with the IASB's revised standards on revenue recognition and leases. We strongly recommend that the Board avoids imposing further significant accounting changes on UK companies within a short time after transition to FRS 102. We therefore recommend that the Board issues supplementary exposure drafts as and when the IASB finalises its standards on revenue recognition and leases.

We believe that there should be a quiet period of at least 18 months between the publication of FRS 102 in final form and its effective date. It may therefore be necessary to defer the effective date of FRS 102 in order that it may reflect the IASB's revised standards on financial instruments, revenue recognition and leases.

We expect that many of our members will be keen to transition to EU adopted IFRS with reduced disclosures as soon as possible in order to achieve consistency with group reporting requirements. We therefore suggest that if there should be a significant delay in finalising FRS 102, the Board should proceed with issuing FRS 101. Moreover, while we recognise that the Board intends to permit early adoption of the new standards, it proposes to restrict early adoption to periods *beginning* after the publication of the final standards. We see no reason why early adoption should not be permitted for periods *ending* after the publication of the new standards.

## **QUESTION 9**

**Do you support the alternative view, or any individual aspect of it?**

We have sympathy with some of the views expressed by the member holding the alternative view. Indeed, we are sure that we have expressed some of the same concerns to the IASB over the years.

We do not believe, however, that the member holding the alternative view appreciates the practicalities of the current situation.

Rightly or wrongly, the Board decided to cease the independent development of UK accounting standards some years ago. As a result, UK accounting standards are now outdated and lack a coherent framework. We accept that, therefore, the most practical alternative available to the Board is to introduce into the UK accounting standards that are based upon IFRS for SMEs. It would simply take too long to develop our own accounting standards.

We recognise that in developing its accounting standards the IASB must consider the views of its international constituents and that it has in place a due process that allows it to gather and understand those views. As a member of the IASB's constituency we seek to influence the IASB's conclusions, but we are not always successful. While we do not always agree with the IASB's conclusions, we are prepared to accept them for so long as they represent a broad consensus.