The Hundred Group
of Finance Directors

Financial Reporting Committee

Jenny Carter
Accounting Standards Board
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17 September 2010

Dear Ms Carter

Assessing the impact of the Accounting Standards Board proposals for the future of UK and Irish Financial Reporting: Request for responses to aid development of the impact assessment on the proposed UK Financial Reporting Framework

Thank you for providing us with an opportunity to comment on the above proposals. Our comments are set out below.

Who we are

The Hundred Group represents the views of the finance directors of the UK's largest companies drawn largely, but not entirely, from the constituents of the FTSE100 Index. Our members are the finance directors of companies whose market capitalisation collectively represents over 80% of that of companies listed on the London Stock Exchange. The views expressed in this letter are not necessarily those of all of our individual members or of their respective employers.

Summary

We set out our responses to the Board's specific questions on in the Appendix.

We are supportive of the approach taken by the ASB, in particular the pragmatic approach taken to disclosure requirements and the endeavours to ensure that the majority of users have a useful, robust and meaningful financial reporting framework to operate within. We are supportive of and appreciate the recognition of the differences in requirements between primary reporters and their subsidiaries, in particular with reference to the users of the accounts.

Our membership consists almost entirely of groups reporting under IFRS. Accordingly, we have focused our responses on the areas of the consultation which will impact our members directly and accordingly have responded to questions 1, 2 and 4. In addition, our comments are focused around 'Tier 1' publicly accountable entities, applying EU-adopted IFRS and their subsidiaries. We make no comments on the wider appropriateness of the developments.

In order to maximise the benefits that will be experienced by our members we look to the development of a reporting regime with recognition and measurement requirements aligned to group reporting for an IFRS group. With this in mind, we would urge the ASB to consider some of the areas where the move to IFRS for a subsidiary would work in direct opposition to this aim, in addition to those areas where we consider the disclosures under IFRS would be particularly burdensome and in some cases meaningless for subsidiaries for example:

- the current requirement to capitalise borrowing costs under IAS23 could require Intercompany interest to be capitalised in the accounts of subsidiaries, which would be eliminated on consolidation.
- The requirement for all entities reporting under IFRS to disclose individual cashflow statements could lead to non-meaningful subsidiary reporting of cashflows given the tendency for cashflows to be managed on a centralised basis for international groups.
- The requirement for defined benefit obligations, where practicable, to be allocated to each reporting entity could also lead to additional, repetitious and in some cases non-meaningful disclosure. Pension schemes are predominantly managed on a country-by-country basis allowing members of pension schemes and investors to review disclosures provided in the Group accounts on a more meaningful basis.
- On a similar basis, share based remuneration schemes are usually run on a country-by-country basis. The Group accounts of most subsidiaries will provide users with in depth disclosure information which would not require repetition in subsidiary accounts.
- Current sensitivity disclosures and other risk disclosures mandated by IFRS7 are more appropriate to Group financial statements, as financial risks are managed predominantly on a Group wide basis, rather than on a subsidiary by subsidiary basis.

In addition, we have regard to the ability to manage our dividend flows to investors and therefore distributable profits. We welcome the Board's review of distributable reserves concerns, and have highlighted the expected depression of distributable reserves that may arise from an increase use of fair value accounting and the requirement for defined benefit pension schemes to be recognised in each entity with employees enrolled in the scheme.

Lastly, but equally importantly, we look to be able to produce financial statements that are focused on key risks to communicate with the stakeholders of each entity. In our opinion the key stakeholders for our subsidiary accounts are usually employees, creditors and, in some cases, a few external investors. These communities are all familiar with the activities of the group and are active users of the internet. We welcome the pragmatic approach taken by the Board when considering the appropriate level of disclosures for subsidiary financial statements and would encourage the board to utilise references to group policies and disclosures where possible to mitigate duplicate information and acknowledge the ease of access to financial reporting that exists.

Please feel free to contact me if you wish to discuss our comments on the proposals.

Yours sincerely

Chris Lucas
Chairman
The Hundred Group - Financial Reporting Committee

APPENDIX

Question 1

Do you have any comments on the overall direction of travel for the UK Financial Reporting Framework as described above?

We are fully supportive of the overall direction of travel for the UK Financial Reporting Framework as set out in the ASB's discussion paper.

In particular, we are supportive of the overall objective of the ASB to embrace International Financial Reporting Standards for the UK, whilst maintaining a pragmatic understanding of the burden of disclosure required by these standards and the usefulness to shareholders and users of the financial statements. In particular we note the understanding of the board of the nature of different stakeholders and users for financial statements depending on the size and nature of the business.

Our comments are made purely with regards to 'Tier 1' entities. Our preferred approach allows UK based subsidiaries of international groups to produce financial statements using the same financial reporting requirements as the group financial statements but with levels of disclosure that reflect their status as part of a larger group and the likely needs of their users. Accordingly we fully support the approach of the ASB to implement a 'reduced disclosure' approach whilst adopting the measurement and recognition requirements of full IFRS.

Question 2

What do you think the overall impact of the proposed UK Financial Reporting Framework will be in terms of its likely costs and benefits – quantified where possible?
In framing your answer you might like to consider the following:
a) the impact on the economy as a whole, efficient functioning of markets and enterprise, fostering investment;
b) transition to the new framework, noting that for entities currently applying the FRSSE there will effectively be no change;
c) the impact on groups of the proposed reduced disclosure framework for subsidiaries;
d) requirements for education and training of account preparers and users, and the impact on their intellectual mobility;
e) whether the information available to users will be more useful for investment decisions, and by owner-managers in managing their businesses, than the existing framework.

Please note that our response relates only to our consideration of Tier 1 entities.

We believe that the proposed changes will be cost beneficial to our members, assuming that a pragmatic approach continues to be taken to disclosure requirements of subsidiaries.

We believe that the ability to utilise one basis for recognition and measurement that is consistent across a Group of companies will save time and reduce costs in the long term.

The ability for entities to produce accounts with reduced disclosure is a pragmatic and appropriate focus for the ASB and one that we support. In particular we support the ASB's consideration for subsidiaries and their stakeholders.

For international groups, in addition to the benefits of having a single financial reporting language, we consider that the changes to IFRS will improve the ability for talented individuals to mobilise across industry but also for our talented individuals to move internationally. This supports our belief that the UK should remain a competitive environment for employers and employees.

We believe that one consistent set of recognition and measurement approaches will be helpful for users of the financial statements who will then be able to assess how the individual entity 'fits in' to the group financial statements. The ability for users to do this, however, will depend on the extent to which the Board addresses any issues which would produce discrepant treatment between the group and subsidiary entities.

Question 4

What do you think the impact of the proposed UK Financial Reporting Framework will be on taxation and distributable profits?

We believe that there will be considerable impact on both taxation and distributable profits for UK entities.

The impact on taxable profits should be discussed with HMRC to ensure that there is mutual understanding of the impact on taxation. Generally we are of the view that transition to IFRS should not cause a material change to the cash tax paid based on HMRC's initiative to ensure that transition should broadly be cash neutral. In addition, assuming that UK GAAP continues to subsume IFRS developments any impact would be a matter of timing rather than fundamental change.

We note that the move to IFRS could also impact deferred taxation calculations for entities, for example under IFRS deferred taxation is recognised for Rolled Over Gains, however are not under UK GAAP. This could lead to an opening adjustment to reserves on transition and a change in the annual rate.

We do not consider either of these points to be insurmountable and are of the opinion that working with HMRC to provide appropriately timed guidance should provide a stable platform for current UK GAAP reporters. The changes to deferred tax and tax rates will provide increase comparability between entities and should be supported.

With respect to distributable profits, we consider that the two predominant impacts for subsidiaries of UK groups will relate to financial instruments and accounting for defined benefit pension schemes.

With respect to financial instruments, the movement to an IFRS basis for recognition and measurement will lead to an increase in fair value measurements within financial statements. The impact of these fair value moments on distributable profits will need to be individually assessed against the distributable profits rules due to the complexity of individual financial instruments. In our assessment, we expect that the increased use of fair value will generally decrease distributable profits in entities on adoption of IFRS. Going forwards the impact will depend on the movements in fair value, but will clearly bring increased uncertainty when performing dividend planning for a group.

With respect to defined benefit pension schemes we note that IFRS does not have the equivalent of the UK multi-employer exemption for subsidiaries. At present under UK GAAP individual entities do not have to account for defined benefit deficits if the pension scheme relates to a number of entities. Under IFRS current requirements there is potential for defined benefit deficits to be introduced to more financial statements, either to a proportionate extent, or with an annual defined contribution-like charge. In both circumstances these adjustments will decrease distributable profits.

It is important for the ASB to consider the implementation date of the change of financial reporting standards. Groups will be required to assess the distributable reserves available under IFRS from the date of transition, not the date of preparation of the financial statements, in order to make a legal dividend for the prior year. This need to understand the impact of transition at the transition date should be emphasised to the market.