

dti

**MODERNISATION OF ACCOUNTING
DIRECTIVES/IAS INFRASTRUCTURE**

A Consultation Document

MARCH 2004



HM TREASURY

MODERNISATION OF ACCOUNTING DIRECTIVES/ IAS INFRASTRUCTURE

A consultation document
on the implementation of
the accounting
modernisation directive
and arrangements for the
use of IAS for companies
and building societies

MARCH 2004

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SECTION 1

Summary and questions

1.1 This consultation covers two broad areas:

- International Accounting Standards (IAS) infrastructure:
 - changes to the Companies Act 1985 (the “1985 Act”) and the Building Societies Act 1986 (the “1986 Act”) to permit companies and building societies to choose whether to switch to IAS;
 - changes to the 1985 Act and the 1986 Act that are necessary to ensure full effectiveness of the IAS Regulation (eg on sanctions);
- changes to the Acts and the Building Societies (Accounts and Related Provisions) Regulations 1998 (the “1998 Regulations”) to implement the Modernisation Directive.

IAS infrastructure – Companies

1.2 One part of this consultation document concerns Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of International Accounting Standards¹ (the “IAS Regulation”) (attached at Annex A).

1.3 Under Article 4 of the IAS Regulation, companies governed by the law of a Member State, whose securities are admitted to trading on a regulated market in any Member State in the European Union (“publicly traded companies”), will be required to prepare their consolidated accounts on the basis of accounting standards issued by the International Accounting Standards Board (IASB)² that are adopted by the European Commission. This will apply to financial years commencing on or after 1 January 2005. The list of regulated markets at 17 February 2004 is set out at Annex B.

1.4 Under Article 5 of the IAS Regulation, use of adopted IAS can be extended on a permissive or mandatory basis. Following a public consultation in 2002³, the Government decided that GB companies would be permitted to choose whether to switch to IAS or continue to prepare their accounts in accordance with the 1985 Act and UK Generally Accepted Accounting Practice (UK GAAP).

1.5 The proposed amendments to the 1985 Act set out a mechanism for companies to choose IAS, provide that companies that make this choice are able to reverse it only in limited circumstances, and require parent companies to ensure consistency of choice within the group unless there are good reasons against it. They are discussed in general terms at paragraphs 4.2 – 4.9 of Chapter 4.

¹ OJ L243/1 of 11 September 2002.

² Accounting standards inherited by the IASB from its predecessor body (including those subsequently modified by the IASB) are called IAS. Completely new standards issued by the IASB will be called International Financial Reporting Standards (IFRS).

³ “International Accounting Standards”, 30 August 2002, URN 02/1158. Available at www.dti.gov.uk/consultations.

1.6 These proposed amendments to the 1985 Act, and the changes that are necessary to ensure full effectiveness of the IAS Regulation, are set out in the draft Regulations at Annex D and discussed in detail in Chapter 5.

1.7 The Charity Commission is not aware of any charities that will be required to use IAS under the IAS Regulation. Although the Government has decided that companies not required to use IAS should be given the choice to do so, it also recognises that special circumstances apply to charities and that IAS was not developed with their needs in mind. On balance, the Government believes the arguments favour not permitting charitable companies to choose to use IAS and does not therefore propose to extend this permission to such companies.

Modernisation Directive – Companies

1.8 The other part of this document concerns Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Council Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings⁴ (the “Modernisation Directive”) (attached at Annex C).

1.9 The Modernisation Directive is designed to bring European accounting requirements into line with modern accounting practices. It requires Member States to make certain changes to national law concerning the form and content of company accounts and the content of the directors’ and auditors’ reports. It also gives Member States options in certain areas.

1.10 The Modernisation Directive must be implemented by 1 January 2005. In Great Britain, this means making amendments to the 1985 Act, by way of secondary legislation.

1.11 The Government’s proposals to implement the Modernisation Directive are discussed in general terms at paragraphs 4.15 – 4.19 of Chapter 4. The proposed amendments to the 1985 Act are set out in the draft Regulations at Annex D and discussed in detail in Chapter 5.

Building Societies

1.12 For the purposes of the IAS Regulation, building societies are covered by the definition of company (see paragraph 3.4), and as a result fall within Article 4 of the IAS Regulation. Consequently, the Government will amend the 1986 Act to ensure that building societies whose securities are admitted to trading on a regulated market in any Member State in the European Union are able to meet the requirements imposed by the IAS Regulation.

⁴ OJ L178/16 of 17 July 2003.

1.13 The Government proposes to permit building societies that do not fall within the mandatory provisions of the IAS Regulation the same choice as companies governed by the 1985 Act. These societies will be able to choose to prepare their accounts in accordance with adopted IAS.

1.14 The Government is also required to implement the Modernisation Directive for building societies. Insofar as the Directive applies to building societies, it is proposed to exercise the Member State options in the same way as for companies. This will involve amendments to the 1986 Act and the 1998 Regulations. These proposals are set out in the draft Order and Regulations for building societies at Annex E and discussed in general terms at paragraphs 4.15 – 4.19 and 4.21 of Chapter 4.

Position of other entities

1.15 For the purpose of the IAS Regulation, industrial & provident societies and friendly societies are also included in the definition of company. HM Treasury intends to issue a separate consultation document later in the year on any changes to legislation for these two categories of entity.

1.16 The Government also intends that the option to use adopted IAS should be extended to Limited Liability Partnerships (LLPs). Appropriate amendments to the relevant legislation will be made in due course.

1.17 The Government also intends that the amendments to be made to the 1985 Act by the regulations at Annex D to implement the Modernisation Directive (the “modernisation amendments”) will apply to LLPs and to certain banking and insurance undertakings (including certain industrial and provident societies and friendly societies) to which Part VII of the 1985 Act is specifically applied. Appropriate amendments to the relevant legislation will be made in due course.

Dividends

1.18 The Government previously consulted on a proposal to amend the provisions in the 1985 Act on presentation and disclosure of dividends⁵. In light of the consultation response to that proposed amendment, the Government is now re-consulting on an amended proposal as part of this consultation. The proposal is discussed in general terms at paragraphs 4.22 and 4.23.

⁵ “Fair Value Accounting”, June 2003, URN 03/960. Available at www.dti.gov.uk/consultations.

Questions for consideration

1.19 In the light of the discussion in the main text of this document, consultees are asked, in particular, to respond to the following questions, **giving reasons for their views:**

1. Do you agree with the policy that the option to choose IAS should operate separately for individual and group accounts?
2. Do you agree with the policy that choice of IAS should be one way, with one exception? Do you think there should be any other exceptions?
3. Do you agree with the policy on consistency of choice of accounting framework within a group?
4. Do you agree with the policy of treating building societies consistently with companies in permitting them to choose to use IAS?
5. Do you agree that charitable companies should not be permitted to choose to use IAS?
6. Do you agree with the Government's proposals to implement (or not implement, as the case may be) the Member State options in the Modernisation Directive for companies and, where applicable, building societies?
7. Do you agree with the Government's proposal on dividends?
8. Do you agree that LLPs, banking undertakings and insurance undertakings should be treated in the same way as Companies Act companies?
9. Can you;
 - (a) identify any costs or benefits for your organisation or more generally resulting from these proposals?
 - (b) quantify those costs or benefits?

See Annex F for details on costs and benefits.

10. Do you have any comments or suggestions on the drafting of the Regulations for companies at Annex D?
11. Do you have any comments or suggestions on the drafting of the Order and Regulations for building societies at Annex E?

Finally, please tell us what your particular interest is, eg are you writing in a personal capacity, or on behalf of a small company, large company, accountancy firm, representative body, etc.

SECTION 2

How to reply

2.1 We invite comments by 2 July 2004 at the latest. Earlier responses would be very welcome.

2.2 Responses should be sent – by email if possible – to the address below. Copies sent by post should be marked “MD/IAS Consultation” on the envelope.

Mrs Valerie Carpenter
Company Law and Investigations Directorate
Department of Trade and Industry
Room 498
1 Victoria Street
London SW1H 0ET

Fax: 020 7215 0235
E-mail: md/ias@dti.gsi.gov.uk

2.3 All responses will be acknowledged. In accordance with the code of practice on open government, comments will be made publicly available unless respondents specifically request otherwise. Any e-mail response sent from a corporate system may carry an automatically generated notice stating that the content of the message should be treated as confidential. If you are replying by e-mail, please make it clear in the body of your response whether or not you wish your comments to be treated as confidential.

Additional copies

2.4 This document is available electronically at www.dti.gov.uk/consultations. You may also photocopy it if you wish, or additional hard copies may be ordered by calling 0870 150 2500 or visiting www.dti.gov.uk/publications.

Questions

2.5 If you have questions about the issues discussed in this consultation document as they relate to companies, please phone Andrew Watchman on 020 7215 0221 or Valerie Carpenter on 020 7215 0225. For questions about the issues as they relate to building societies, please phone Ian Noon on 18002 020 7270 5897 (please dial the whole number).

SECTION 3

Background

International Accounting Standards

3.1 The IAS Regulation introduces important changes which will directly affect the way in which certain companies across the EU prepare their financial statements. As a minimum, it will require publicly traded companies governed by the law of a Member State to prepare their consolidated accounts on the basis of accounting standards issued by the IASB that are adopted by the European Commission. To date, all IAS in existence at 1 May 2002 have been adopted with the exception of IAS 32 (*Financial Instruments: Disclosure and Presentation*) and IAS 39 (*Financial Instruments: Recognition and Measurement*). Those standards and other new and revised standards will be considered for adoption by the Commission. The first of the new standards, IFRS 1 (*First Time Adoption of International Financial Reporting Standards*), has also been adopted. The IAS Regulation will apply to financial years commencing on or after 1 January 2005.

3.2 Member States have the option to extend the application of the Regulation. They may **permit** or **require**:

- publicly traded companies to prepare their individual accounts in accordance with adopted IAS;
- some or all non-publicly traded companies to prepare their consolidated and/or individual accounts in accordance with adopted IAS.

3.3 The Government announced on 17 July 2003 that the application of the Regulation will be extended so that:

- publicly traded companies will be **permitted** to use IAS in their individual accounts; and
- non-publicly traded companies and LLPs will be **permitted** to use IAS in both their individual and consolidated accounts.

3.4 For the purposes of the IAS Regulation, “company” has the same meaning as in Article 48 (old Article 58) of the Treaty of Rome:

“Companies or firms” means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making”.

3.5 For the purposes of the extension to the application of the IAS Regulation to be effected by the draft Regulations at Annex D, “company” means companies required to prepare accounts by the 1985 Act (although the Government also proposes to extend the application of the IAS Regulation to building societies formed under the 1986 Act and to LLPs and certain banking and insurance undertakings to which Part 7 of the 1985 Act is specifically applied).

3.6 To determine whether they are subject to Article 4 of the IAS Regulation, publicly traded companies need first to establish whether they are required by the 1985 Act (which implements the Seventh Directive on consolidated accounts⁶) to prepare group accounts. If they are, then adopted IAS will apply to such accounts.

3.7 For companies using adopted IAS, either because they fall within Article 4 of the IAS Regulation or because they have chosen to do so under Article 5 as it is to be implemented in the 1985 Act, certain parts of the 1985 Act concerning the content and format of accounts will no longer apply. Other parts of the 1985 Act relating to accounting and reporting will continue to apply. In broad terms, where IAS is used, the detailed requirements of the 1985 Act regarding the form and content of accounts will not apply. However, the basic requirement to prepare accounts, including the circumstances in which consolidated accounts are required, as well as requirements on audit, approval, distribution to members and filing, will continue to apply to all companies. Also, information outside the scope of IAS and required by the 1985 Act to be included in the annual report and accounts, such as information on directors' remuneration and the contents of the directors' report, will not be affected by IAS.

3.8 Guidance from the European Commission on the interaction between the IAS Regulation and the Accounting Directives can be found at http://www.europa.eu.int/comm/internal_market/accounting/docs/ias/200311-comments/ias-200311-comments_en.pdf.

3.9 Statements of Recommended Practice (SORPs) give guidance on the application of UK accounting standards to particular industries or sectors, for example charities, insurance business and investment trusts. Compliance with the relevant SORP is not mandatory but those that do not comply are required (by Financial Reporting Standard 18: *Accounting Policies*) to explain why. It is likely that SORPs will be less relevant and have a significantly reduced status in an IAS regime. IAS at present includes little or no guidance at a sectoral level similar to SORPs. SORPs may have a useful ongoing role as guidance, but only to the extent that they do not conflict with adopted IAS.

3.10 The Government is aware that there is concern about the ability of companies using IAS to continue to produce Summary Financial Statements as set out in the 1985 Act. Separately from this consultation, consideration will be given to how the concept of Summary Financial Statements can be retained under IAS.

3.11 Ultimately, it would be preferable for all British companies to use the same accounting standards. The impact of the IAS Regulation will be reviewed after 2008 to establish if it would be appropriate to mandate wider use of IAS. This will depend in part on the development of a regime for

⁶ Seventh Council Directive of 13 June 1983 (83/349/EEC) based on Article 54(3)(g) of the Treaty on consolidated accounts. OJ L193/1 of 18 July 1983.

smaller companies. At present, IAS does not offer a simplified regime for smaller companies comparable to that in the UK. The IASB is currently working on this issue.

3.12 Article 9 of the IAS Regulation gives Member States an option to extend from 2005 to 2007 the deadline for using IAS for two classes of company. This covers companies with listed debt securities only, and companies admitted to trading outside the EU using internationally accepted standards for that purpose. As indicated in the August 2002 DTI consultation document "International Accounting Standards", the Government does not intend to take up this option.

Modernisation Directive

3.13 EU accounting requirements are based primarily on the four Accounting Directives: that is to say, the Fourth⁷ and Seventh Directives on the annual and consolidated accounts of companies; the Directive on the annual and consolidated accounts of banks and other financial institutions⁸ (the Bank Accounts Directive); and the Directive on the annual and consolidated accounts of insurance undertakings⁹ (the Insurance Accounts Directive).

3.14 The Modernisation Directive amends the Accounting Directives. It is designed to:

- remove conflicts between the Accounting Directives and IAS in existence at the time it was drawn up; and
- ensure that optional accounting treatments available under IAS in existence at 1 May 2002 are available to EU companies which continue to have the Accounting Directives as the basis of their accounts (ie those companies which will not prepare their accounts in accordance with the IAS Regulation).

3.15 The Modernisation Directive also amends the Insurance Accounts Directive to allow Member States to permit or require insurance companies to account at fair value for some of their financial instruments. These provisions will be taken forward with the Fair Value Directive¹⁰, which covers fair value accounting for financial instruments in respect of other companies. The DTI consulted on proposals for implementing this Directive last year¹¹. The Fair Value Directive will be implemented later this year in regulations that will be combined with the final version of the Regulations at Annex D. It is intended that the Fair Value amendments will also have effect for financial years beginning on or after 1 January 2005.

⁷ Fourth Council Directive of 25 July 1978 (78/660/EEC) based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies. OJ L222/11 of 14 August 1978.

⁸ Council Directive of 8 December 1986 (86/635/EEC) on the annual accounts and consolidated accounts of banks and other financial institutions. OJ L372/1 of 31 December 1986.

⁹ Council Directive of 19 December 1991 (91/674/EEC) on the annual accounts and consolidated accounts of insurance undertakings. OJ L374/7 of 31 December 1991.

¹⁰ Directive 2001/65/EC of the European Parliament and of the Council of 27 September 2001 amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions. OJ L 283/28 of 27 October 2001.

¹¹ "Fair Value Accounting", June 2003, URN 03/960. Available at www.dti.gov.uk/consultations.

3.16 The Modernisation Directive includes amendments to the requirements regarding the annual report (referred to in the 1985 Act and the 1986 Act as the directors' report). These are being dealt with separately for companies and building societies. For companies, there are some similarities between these provisions and the Government's proposals for a statutory Operating and Financial Review (OFR). Therefore, these particular amendments from the Modernisation Directive are being taken forward with the OFR proposals for companies, which will shortly be the subject of a separate public consultation. The intention is that the OFR and directors' report regulations, the Regulations at Annex D and the Fair Value regulations will be brought together as a single statutory instrument later this year. However, for building societies, these amendments to the requirements regarding the annual report are being taken forward as part of this consultation.

3.17 Apart from the amendments to the audit requirements (paragraphs 5.16 – 5.17) and to the circumstances in which companies are required to prepare group accounts (paragraphs 5.11 – 5.15 and 5.18 – 5.19), the amendments covered by this part of the consultation will not directly affect the consolidated accounts of those companies subject to the IAS Regulation (ie publicly traded parent companies) after 2004, because from 1 January 2005 adopted IAS will replace all the detailed **accounting** provisions of the 1985 Act for such companies. The accounts of any companies that choose to use IAS under the extension of the IAS Regulation will also fall outside the detailed accounting provisions of the 1985 Act (see paragraph 3.7 above).

The ASB's Convergence Programme

3.18 The Accounting Standards Board's (ASB) standards will continue to apply to all UK companies, building societies and certain other reporting entities that do not report under the IAS Regulation (whether directly or by extension). The ASB does not believe it is a credible option, except in the short term, to retain two different sets of standards in use in the UK. It therefore aims to bring UK standards into line with IASB standards. It will be issuing a consultation paper shortly setting out proposals for achieving this.

Taxation

3.19 On 17 March 2004, the Chancellor of the Exchequer confirmed in his Budget (Budget Note REV BN25) the announcement made in his Pre-Budget Report (10 December 2003) that those companies that choose to use IAS in their individual accounts will be able to use those accounts as the starting point for their tax computations, and will not have to prepare separate UK GAAP accounts just for tax purposes.

3.20 The Budget said that Registration will be included in the Finance Bill 2004 to:

- ensure that accounts prepared in accordance with either IAS or UK GAAP will be an acceptable starting point for computing taxable profits;
- ensure the R&D tax rules continue to allow the special reliefs and credits in the year in which expenditure is incurred, whatever the accounting treatment;
- continue the current tax treatment of most hedging arrangements using derivative contracts and foreign currency liabilities; and
- amend the corporate debt and derivative contracts legislation to reflect the changes made by IAS 39 and complementary revisions to UK accounting standards.”

3.21 That work is continuing, and further information is available on the Inland Revenue website <http://www.inlandrevenue.gov.uk>.

Charities

3.22 The accounting provisions of Part 7 of the 1985 Act apply to charitable companies. The SORP “Accounting and Reporting by Charities” (published by the Charity Commission in October 2000 and updated in January 2003) supplements accounting standards and other legal and regulatory requirements in the light of the special factors prevailing or transactions undertaken within the charities sector. The SORP applies to charities, however constituted, throughout the UK unless a more specialised SORP applies as in the case of Higher and Further Education Institutions or for Registered Social Landlords. SORPs provide a unified approach to charity sector accounting and are developed to meet criteria laid down by the ASB in conformity with the ASB’s code of practice, given in the ASB Statement of 27 July 2000 “SORPs: Policy and Code of Practice”. In the UK, the SORP-making body for general charities is the Charity Commission.

SECTION 4

Proposals – Policy

IAS infrastructure

Companies

4.1 Publicly traded British companies that are required to prepare consolidated accounts will be required by the IAS Regulation to prepare those consolidated accounts in accordance with IAS for financial years beginning on or after 1 January 2005. The IAS Regulation is directly applicable in national law without additional implementing provisions, other than those necessary to ensure it is fully effective.

4.2 However, for companies that will be permitted to use IAS under the extension of the IAS Regulation, it is necessary to include specific provisions in the 1985 Act to allow that choice to be made.

4.3 The Government intends that the option to choose IAS will operate separately for individual accounts and for group accounts (where such group accounts are required and are not caught directly by Article 4 of the IAS Regulation). In other words, a parent company can elect to use IAS for its group accounts without having to use IAS for its individual accounts, and vice versa. The Government considers that it would be quite rare for a parent company to choose IAS for its consolidated accounts but not its individual accounts, or vice versa. However, a flexible approach was widely supported by respondents to the 2002 DTI consultation “International Accounting Standards”.

1. Do you agree with the policy that the option to choose IAS should operate separately for individual and group accounts?

4.4 The Government proposes that this choice should be “one way”. In other words, once having chosen to use IAS, companies cannot reverse that choice. This will ensure that companies do not use the permission to misrepresent their position by switching between regimes depending on which shows their performance in a better light. One exception to this is proposed: if a company becomes a subsidiary of an EEA undertaking that does not prepare its individual accounts in accordance with the IAS Regulation. It would not be appropriate to require the subsidiary to continue to use IAS if the parent did not use IAS.

2. Do you agree with the policy that choice of IAS should be one way, with one exception? Do you think there should be any other exceptions?

4.5 The Government believes that it would be desirable for the individual accounts of all companies in a group to be prepared using the same set of accounting standards. This has the benefit of maximum consistency and transparency. The use of different standards within a group could also provide opportunities for tax avoidance.

4.6 However, imposing an absolute requirement for consistency within a group has drawbacks. Individual companies in a group may not all be equipped to switch to IAS at the same time; requiring them to do so could impose an unreasonable burden which would only serve to discourage the use of IAS. There are also definitional issues; a parent company of a group as defined in the 1985 Act might not in every case have sufficient control to force a subsidiary to change its accounting framework.

4.7 The Government therefore proposes including a provision that a parent company shall ensure that the individual accounts of its subsidiary undertakings are prepared using an accounting framework consistent with the individual parent company accounts unless there are good reasons against it. There would be an exception to this provision for parent companies required under the IAS Regulation to prepare their group accounts in accordance with IAS, who choose to present their individual accounts under IAS for consistency. In that case, the parent company need not ensure that all its subsidiaries use IAS, but should still ensure that the subsidiaries are consistent with one another.

4.8 This limited exemption is proposed on the basis that parent companies that are obliged to use IAS for their consolidated accounts should not be deterred from using IAS in their individual accounts. Given that the consolidated and individual accounts will be presented in the same annual report, the use of the same basis for both will avoid unnecessary confusion and have practical advantages in presentation. The Government therefore considers that parent companies that take this approach should not be obliged to switch all of their GB subsidiaries' accounts to IAS as a consequence.

4.9 It is not proposed to extend this exemption to parent companies that will have the choice between UK GAAP and IAS in their consolidated accounts. This is on the basis that such companies will be in a position to switch to IAS at a time of their choosing. The Government considers that such a switch should usually be made at the same time for the consolidated accounts, the parent's individual accounts and the GB subsidiaries' accounts.

3. Do you agree with the policy on consistency of choice within a group?

Building Societies

4.10 The IAS Regulation imposes the same requirements on building societies with publicly traded securities as it does on publicly traded companies; those societies must use IAS for their consolidated accounts. For the purposes of the extension to the application of the Regulation, the Government believes that there should be consistency between companies and building societies. In line with the policy towards companies, it is therefore proposed that building societies should have the option of using IAS (where they are not required to do so) for their consolidated and individual accounts, that the choice to use IAS cannot be reversed and that there should be consistency of choice within a group.

4.11 For companies, there will be an exception to the rule that once a company has chosen to use IAS it cannot go back to preparing its accounts under the 1985 Act (see paragraph 4.4 above). However, because it is not legally possible for building societies to become subsidiaries, there will be no exception provided in these terms to permit building societies to return to the existing accounting regime once they have gone over to IAS accounts.

4. Do you agree with the policy of treating building societies consistently with companies in permitting them to choose to use IAS?

Charitable companies

4.12 There is also a question of whether charitable companies governed by the 1985 Act should be allowed to use IAS. All else being equal, it would be desirable to treat all classes of company in the same way. Increasingly, it is recognised that the same fundamental principles of accounting should be applied both to the profit and not-for-profit sectors.

4.13 On the other hand, IAS has to date been designed for use in the for-profit sector. Particular issues arise in the context of charity accounting. Although charitable companies comply with UK accounting standards, they also follow the extra guidance given in the SORP "Accounting and Reporting by Charities". It is likely that SORPs will be less relevant and or have a significantly reduced status in an IAS regime. IAS does not specifically address certain charity sector transactions, and the direct application of IAS without modifications through a SORP might create interpretational issues in presenting accounts fully and fairly. There are no plans to permit non-company charities to use IAS. Adoption of IAS by charitable companies would therefore be likely to lead to a loss of consistency within the charitable sector. Overall, the effect might be to damage public confidence in the accounting framework for the charitable sector.

4.14 On balance, the Government believes the arguments favour not permitting charitable companies to use IAS in either their individual or consolidated accounts. Therefore, it does not propose to extend the permission to charitable companies.

5. Do you agree that charitable companies should not be permitted to use IAS?

Modernisation Directive

4.15 Directives are not directly applicable in Member States and must be implemented through national law. The Government's general approach to implementing the Modernisation Directive is to facilitate greater convergence between UK accounting standards and IAS, without imposing unnecessary burdens.

4.16 The Directive gives Member States options in seven of its accounting provisions. The Government is proposing to take up two of the options as follows:

- the presentation of items within the balance sheet and profit and loss account must have regard to the substance of the reported transaction or arrangement (originally proposed as part of the implementation of the Fair Value Directive); and
- all companies will be permitted to account for investment property and biological assets at fair value (with fair value changes to be reported in the profit and loss account), in both their annual and consolidated accounts.

4.17 These options are discussed in more detail in paragraphs 5.27 – 5.29 and 5.31 – 5.34 respectively.

4.18 In addition, the Government is now proposing to take up an existing Member State option in the Seventh Directive to exempt a parent company governed by GB law, which is also a subsidiary company of a parent company not governed by EEA law, from the requirement to prepare consolidated accounts, subject to various conditions. This is discussed in more detail at paragraphs 5.11 – 5.13.

4.19 Finally, there are five Member State options the Government does not plan to take up:

- Member States may permit or require additional statements to be provided in annual accounts. The European Commission has specifically identified a cash flow statement as an example of an additional statement. The Government believes that cash flow statements are an important element of financial statements and are generally necessary in order that the statements give a true and fair view. However, as this area is already dealt

with in accounting standards, the Government is not proposing to make it a specific legal requirement.

- Member States may permit or require companies to draw up a balance sheet that presents items on the basis of a distinction between current and non-current items, as an alternative to the current balance sheet layouts. The Government considers that this option would cause confusion and lack of consistency in the absence of an accounting standard to clarify its use, and that any benefit from its adoption would be minimal.
- Member States may permit or require companies to present a statement of their performance instead of a profit and loss account, provided the information given is at least equivalent. As the timing of the IASB's project on comprehensive income is uncertain, the Government believes it is inappropriate at the current time to require or permit companies to prepare such statements.
- Member States may permit or require account to be taken of all foreseeable liabilities and potential losses in addition to all liabilities arising. The Government considers that this situation is already sufficiently covered by the current wording in the 1985 Act.
- Member States may permit or require insurance companies to use different valuations for different elements of certain investments. The Government believes that, as insurance standards are in a state of transition, it would be more appropriate to consider this when the situation is more settled.

4.20 Other parts of the Directive that are not being implemented are discussed at paragraphs 4.32 – 4.39.

4.21 In line with the policy of consistency between companies and building societies in accounting matters as far as possible, the Government proposes to deal with the Member State options for building societies in the same way as for companies. The exception is the option discussed at paragraph 4.18; as mentioned previously, it is not legally possible for building societies to operate as subsidiaries of a parent undertaking.

6. Do you agree with the Government's proposals to implement (or not implement, as the case may be) the Member State options in the Modernisation Directive for companies and, where applicable, building societies?

Dividends

4.22 As part of the consultation on implementing the Fair Value Directive, the Government proposed to amend the 1985 Act so that companies would no longer be required to show dividends that did not represent a liability at year-end in the profit and loss account. The proposed amendment attracted considerable comment. Many consultees did not support the amendment as proposed, and there were a number of alternative suggestions.

4.23 The Government has taken account of these comments and now proposes a revised amendment. Rather than paid and proposed dividends, companies will be required to show in the profit and loss account “dividends paid (other than those for which a liability existed at the immediately preceding balance sheet date) or liable to be paid”. In the notes to the accounts, all companies (including small) will be required to show the aggregate amount of any dividends proposed before the date of approval of the accounts, which have not otherwise been shown in the profit and loss account. The revised proposal is still in line with current international practice in this area.

7. Do you agree with the Government’s proposal on dividends?

LLPs, banking undertakings and insurance undertakings

4.24 The Limited Liability Partnerships Regulations 2001¹² apply the accounting provisions in Part VII of the 1985 Act to LLPs. Subsequent amendments to the provisions of Part VII that are applied to LLPs will, unless a contrary intention appears in the later legislation, apply automatically to LLPs.

4.25 The Government’s general policy on LLPs is to treat them in the same way as companies of the same size and sector unless this is clearly inappropriate. It proposes, therefore, that the amendments to be made by the Regulations at Annex D should apply to LLPs, with any necessary modifications.

4.26 Similar considerations apply to those banking and insurance undertakings (including certain industrial and provident societies and friendly societies) to which Part VII is applied by the Bank Accounts Directive (Miscellaneous Banks) Regulations 1991¹³ and the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 1993¹⁴.

4.27 Regulations making any necessary modifications in respect of LLPs and banking and insurance undertakings will be made after the Regulations at Annex D.

8. Do you agree that LLPs and banking and insurance undertakings should be treated in the same way as Companies Act companies?

¹² S.I. 2001/1090.

¹³ S.I. 1991/2704.

¹⁴ S.I. 1993/3245.

Regulatory Impact Assessments

4.28 Separate draft Regulatory Impact Assessments for the Modernisation Directive and IAS aspects of the regulations can be found at Annex F. These attempt to identify and quantify the costs and benefits of the proposals.

9. Can you:

(a) identify any costs or benefits for your organisation or more generally resulting from the proposals in this consultation document?

(b) quantify those costs or benefits?

See Annex F for details on costs and benefits.

Provisions of the Modernisation Directive being implemented separately

Articles 1.14, 1.17 and 2.10(a)

4.29 For companies, these Articles are being implemented through the OFR and directors' report regulations (for building societies, they are included in this consultation).

Article 4.2

4.30 These amendments relate specifically to the Lloyd's insurance market and are being taken forward separately by HM Treasury.

Article 4.5

4.31 The provisions on fair value accounting for financial instruments for insurance companies were consulted on in summer 2003 as part of the consultation on implementing the Fair Value Directive. The Fair Value regulations and the Regulations at Annex D will be laid before Parliament as a single set of regulations in the autumn. It is also intended that the Fair Value regulations for building societies and the Regulations at Annex E will be laid before Parliament in the autumn.

Significant provision of the Modernisation Directive not being implemented

Articles 1.1 (individual companies) and 2.7 (groups)

4.32 These Articles in the Modernisation Directive give Member States the option to permit or require additional statements (the European Commission has identified a cash flow statement as an example) to be provided in the annual accounts. UK companies already provide a cash flow statement (other than in limited circumstances where exemptions apply) because of a requirement in UK accounting standards.

Articles 1.6 (1.3, 1.13, 1.21 are linked to Article 1.6) and 3.3 (banks)

4.33 Member States may permit or require companies to draw up a balance sheet on the basis of a distinction between current and non-current items, provided the information given is at least equivalent to that required by the balance sheet formats in Articles 9 and 10 of the 4th Directive (and imported into the 1985 Act). IAS does not include requirements for specific balance sheet formats to be used. In the absence of a generally accepted approach to the presentation of balance sheets on the basis of current and non-current items, taking up this option could cause confusion and reduce comparability. Complication would arise because of the various cross-references in the provisions of the 1985 Act to items in the existing formats. Any benefit from its adoption would be minimal.

Articles 1.8 and 3.4 (banks)

4.34 These Articles give Member States the option to permit or require companies and banks to present a statement of their performance instead of a profit and loss account, provided the information given is at least equivalent (a performance statement might include gains and losses which are currently shown in a statement other than the profit and loss account). As it is presently unclear when the IASB may publish an accounting standard on reporting comprehensive income, it is inappropriate at the current time to require or permit companies to prepare such statements.

Article 1.9

4.35 This Article gives Member States the option to permit or require account to be taken of all foreseeable liabilities and potential losses in addition to all liabilities arising. We believe the current wording in the 1985 Act is consistent with modern accounting practices and that this Member State option might, if taken up, blur the distinction between actual and contingent liabilities for accounting purposes.

Article 1.10

4.36 This Article allows Member States to permit the revaluation of any fixed asset, including intangibles. Paragraph 31 of Schedule 4 already permits intangible assets (other than goodwill) to be included at their current cost.

Articles 1.20, 2.3(a) and 2.12

4.37 Companies whose securities are admitted to trading on a regulated market of any Member State may no longer apply for exemption from certain obligations. This reflects the existing position under the 1985 Act.

Article 1.22

4.38 This amends terminology in the Fourth Directive from “market value” to “fair value”. We believe the two terms have the same meaning for all practical purposes.

Article 4.4

4.39 This Article gives Member States the option to permit or require insurance companies to use different valuations for different elements of certain investments. At this stage, we do not propose to exercise this option. Accounting standards for insurance are in a state of transition and it is considered more appropriate to amend the law when the international position is settled.

SECTION 5

Proposals for companies – Detail

The Draft Regulations

5.1 This section acts as an explanatory note to the draft Regulations, explaining the purpose and intention of each regulation.

5.2 The Regulations are divided into three parts. Part 1 (Regulation 1) is introductory. Part 2 (Regulations 2 and 3) covers amendments to the sections of the 1985 Act, relating to the use of IAS. Part 3 (Regulations 4 – 11) covers amendments to the sections of the 1985 Act to implement the Modernisation Directive and related proposals.

5.3 There are also a number of Schedules immediately following Part 3 of the draft Regulations. Schedule 1 contains consequential amendments to the 1985 Act as a result of accounts being prepared using IAS. Schedules 2 – 6 contain specific amendments to the Schedules to the 1985 Act and Schedule 7 contains minor and consequential amendments as a result of the Modernisation Directive and related provisions. Following consultation, and when they are combined with the Fair Value and OFR and directors' report regulations, consideration will be given to some amalgamation of these Schedules to make them more accessible to users.

Part 1 of the draft Regulations

Regulation 1

5.4 Regulation 1 provides for the Regulations to come into force on the day after the day on which they are made, and to apply to financial years starting on or after 1 January 2005. This includes financial years which would have started on or after that date as a result of a company using the power in section 223 of the 1985 Act to change its accounting year.

Part 2 of the draft Regulations

Regulation 2

5.5 Regulation 2 replaces existing sections 226 and 227 of the 1985 Act (duty to prepare individual and group accounts) with new sections 226 to 226B and 227 to 227C which reflect the fact that some companies will continue to prepare their accounts in accordance with the 1985 Act and others will use IAS as adopted by the European Commission pursuant to the IAS Regulation. Much of existing sections 226 and 227 are re-enacted.

5.6 This regulation gives effect to the Government's policy of permitting choice in use of IAS. New section 226(2) provides that all companies can choose to prepare their individual accounts in accordance with the detailed accounting provisions of the 1985 Act or with adopted IAS. New section 227(2) and (3) reflect the fact that publicly traded companies will be required to prepare their consolidated accounts in accordance with adopted IAS, and provides that non-publicly traded companies can choose to prepare their consolidated accounts in accordance with the 1985 Act or with adopted IAS. Charitable companies will not be permitted to use IAS (section 226(3), 227(4) and 227C(2)).

5.7 Section 227C provides that parent companies shall, in most circumstances, ensure that the individual accounts of the parent company and the individual accounts of subsidiary undertakings (where these are required to be prepared under Part VII of the 1985 Act) within the group are prepared using the same financial reporting framework (ie. either adopted IAS or UK GAAP), unless there are good reasons for not doing so. However, the individual accounts of any undertaking that is a charity do not have to be prepared on the same basis as the other individual accounts in the group. Nor do the individual accounts of the subsidiaries have to be prepared using the same financial reporting framework as those of a parent company where the parent company is required by the IAS Regulation to use adopted IAS for its consolidated accounts, and has chosen to do so for its individual accounts.

5.8 In the interests of consistency and comparability, it is also proposed (in sections 226(4) and (5) and 227(5) and (6)) that companies choosing to prepare their accounts under IAS must continue to do so in subsequent financial years. However, this requirement will not apply if a company preparing accounts under IAS becomes a subsidiary of an EEA undertaking which prepares accounts on a non-IAS basis.

5.9 To aid users of accounts, it is proposed (in sections 226B and 227B) that companies preparing accounts under IAS should be required to disclose this fact in the notes to their accounts.

Regulation 3

5.10 The regulation introduces Schedule 1 to the Regulations which contains consequential amendments to the 1985 Act as a result of accounts being capable of being prepared either under the 1985 Act or under IAS.

Part 3 of the draft Regulations

Regulation 4

5.11 This regulation implements an option in Article 11 of the Seventh Directive, not hitherto exercised in the 1985 Act. Article 11 gives a Member States an option to exempt any intermediate parent company governed by its law from the requirement to prepare consolidated accounts, if that company is a subsidiary of another undertaking not governed by the law of an EEA State, provided certain conditions are fulfilled.

5.12 In order to align the exemptions from preparation of consolidated accounts more closely with those in IAS 27 (*Consolidated Financial Statements and Accounting for Investments in Subsidiaries*), the Government now wishes to take up this further exemption option in the Seventh Directive. The latest version of IAS 27 allows an exemption from the requirement to prepare consolidated accounts for an intermediate parent company wholly owned by a parent company that draws up consolidated accounts in accordance with IAS (subject to certain other conditions). However, under the 1985 Act, a group of companies whose parent is wholly-owned by a non-EU parent company would be required to prepare consolidated accounts, even if electing to follow IAS and meeting the exemption criteria in IAS 27.

5.13 Regulation 4 inserts new section 228A into the 1985 Act. It provides for the new exemption and sets out the conditions that must be fulfilled for exemption. One of the more important conditions is that the higher parent company presents consolidated financial statements in a manner equivalent to the Seventh Directive. We would expect that, in most circumstances, financial statements prepared on the basis of IAS would meet this equivalence condition. The new exemption will be restricted to wholly-owned intermediate parent companies to be consistent with the conditions in IAS 27.

Regulation 5

5.14 This regulation implements Article 2.6 of the Modernisation Directive, which deletes Article 14 of the Seventh Directive, by repealing section 229(4) of the 1985 Act. Article 14 had provided for the exclusion of an undertaking from the consolidated accounts of the parent if its activities were so incompatible with those of the parent that inclusion would fail to meet the requirement to give a true and fair view of the undertakings included therein, taken as a whole. This provision is in conflict with IAS 27, which does not permit any exclusion on the ground of incompatible activities.

5.15 In addition, we have taken this opportunity to bring the 1985 Act into line with the Seventh Directive by permitting a subsidiary undertaking to be excluded from consolidation where the parent company's interest in it is held exclusively with a view to subsequent resale irrespective of whether or not it

has previously been included in consolidated accounts. This also brings the law more into line with the requirements of IAS 27.

Regulations 6, 7 and 8

5.16 These regulations implement Articles 1.15, 1.16 and 1.18 of the Modernisation Directive concerning the audit report of individual companies, and Article 2.11 concerning the audit report of groups.

5.17 By specifying matters to be covered in auditors' reports, Articles 1.15 and 1.18 of the Modernisation Directive seek to achieve greater harmonisation and reflect best practice concerning the format and content of audit reports, which currently differ across Member States. Audit reports prepared in accordance with UK Statement of Auditing Standards 600 already conform very closely to the requirements of the Modernisation Directive. One of the more significant changes in the statutory requirements is that, in future, the auditors will need to identify the financial reporting framework applied in the preparation of the accounts (ie whether IAS or UK GAAP). Regulation 8 amends section 240(d) of the 1985 Act in implementation of Article 1.16 of the Modernisation Directive. This requires disclosure, whenever non-statutory accounts are published, of whether the auditors have drawn attention in their report to any matter by way of emphasis, without qualifying the audit report, as well as of whether the audit report was qualified or unqualified.

Regulation 9

5.18 This regulation implements Article 2.1 of the Modernisation Directive, which is designed to align the Seventh Directive with IAS requirements. Under IAS 27, an undertaking is a subsidiary undertaking if it is controlled by a parent, irrespective of the existence of an interest in the capital of the undertaking. The current requirement in the Seventh Directive for a participating interest to exist is, therefore, removed. Accordingly, the requirement in section 258(4) of the 1985 Act for a participating interest to exist in order for an undertaking to be a subsidiary is also removed.

5.19 The Modernisation Directive did not remove the requirement for a participating interest to exist in the definition of an associate (see paragraph 20 to Schedule 4A to the 1985 Act). On the face of it, it would appear sensible to align the definitions of subsidiary and associate in this respect. Under IAS 28 (*Accounting for Investments in Associates*), an undertaking is an associate of an investor if the investor can exercise significant influence, irrespective of the existence of a participating interest. The Government would be interested in consultees' comments on this, with a view to future amendments to the Accounting Directives.

Regulation 10

5.20 Regulation 10 identifies the 5 Schedules to the 1985 Act which require amendment to implement the Modernisation Directive and related provisions. The amendments to the Schedules (listed as Schedules 2 – 6 after Part 3 of the draft Regulations) are discussed below.

Schedule 1 to the draft regulations (Regulation 3)

5.21 The necessary minor and consequential amendments to the 1985 Act to take account of the use of IAS are set out in Schedule 1. The significant consequential amendments are discussed below.

Paragraph 8

5.22 This paragraph re-enacts the existing disclosure requirements regarding particulars of staff in paragraph 56 of Schedule 4 to the 1985 Act. It is being removed from Schedule 4 and inserted as section 231A in Part VII of the 1985 Act because these disclosures will also have to be given by a company preparing accounts in accordance with adopted IAS.

Paragraphs 13 and 15

5.23 These paragraphs amend sections 247 and 249 of the 1985 Act regarding the qualification of a company or a group as small or medium-sized. They provide that where a company or group prepares accounts under IAS, it can qualify as small or medium-sized if it meets the threshold requirements on the basis of amounts extracted from accounts prepared in accordance with adopted IAS. At present, sections 247 and 249 refer to specific line items within the accounts formats, which will not apply to accounts prepared under adopted IAS.

Schedule 2 to the draft regulations (Regulation 10(1))

5.24 This amends Schedule 4 to the 1985 Act. Schedule 4 contains the requirements on the form and content of the individual accounts of large and medium sized “ordinary” companies (that is to say, companies which are neither banks nor insurance companies).

Paragraph 2

5.25 This is not part of the package of Modernisation Directive amendments. Rather, it relates to dividends, and is designed to facilitate the ASB’s programme of convergence with IAS. The Government consulted on a previous version of these amendments with the proposals for implementing the Fair Value Directive. The proposal was amended as a result of comments received.

5.26 This part of the draft Regulations amends paragraph 3(7) of Schedule 4 to the 1985 Act, by replacing the requirement for companies to show paid and proposed dividends as separate items in the profit and loss account, with a requirement to show dividends which are paid or liable to be paid at the balance sheet date. However, the amount of any proposed dividend is important for shareholders and other users of accounts. Therefore, it is proposed to introduce a new requirement, as paragraph 3(7A), to disclose in the notes to the accounts the aggregate amount of dividends proposed before the date of approval of the accounts, which have not been shown in the profit and loss account in accordance with the new requirement in paragraph (3)(7)(b).

Paragraph 3

5.27 This implements Article 1.2 of the Modernisation Directive. Member States may permit or require the presentation of amounts within items in the profit and loss account and balance sheet to have regard to the substance of the reported transaction.

5.28 This is a key element in the convergence of UK accounting standards to IAS in the area of financial instruments. It will permit compliance with IAS 32. The Government proposes to implement this as a requirement rather than a permission so that accounts must reflect the substance of the transaction. It is important that formats do not create excessive rigidity and become an obstacle to presenting items in the most meaningful way.

5.29 The insertion of a new paragraph 5A on presentation of items in Schedule 4 to the 1985 Act amends the existing requirements so that the presentation of items within the formats must have regard to their economic substance.

Paragraphs 4, 5, 9, 10 and 12

5.30 These paragraphs implement Articles 1.4, 1.5, 1.7, 1.9 and 1.11 of the Modernisation Directive. They make minor changes in the terminology relating to provisions to align with IAS 37 (*Provisions, Contingent Liabilities and Contingent Assets*).

Paragraphs 6, 7, 8 and 11

5.31 These paragraphs implement the Member State option in Article 1.12 of the Modernisation Directive. The Fair Value Directive amended the Accounting Directives to permit certain financial instruments to be recorded at fair value in accordance with IAS 39. To deal with future developments, the Modernisation Directive gives Member States the option to extend use of fair value accounting to other asset categories, and to restrict its use to consolidated accounts.

5.32 The IAS on investment property (IAS 40 *Investment Property*) and living animals and plants (IAS 41 *Agriculture*) have been adopted pursuant to the IAS Regulation. Therefore, the Government has decided to permit these categories of assets to be fair valued in both individual and consolidated accounts. This will facilitate convergence with IAS, and the optional approach is in line with the proposed policy on fair value accounting for financial instruments.

5.33 New paragraphs 34CA and 45D and amended paragraph 34D of Schedule 4 to the 1985 Act implement this policy, and set out certain rules for the use of fair value in these circumstances. The amendments should therefore be looked at in the context of the draft regulations in the Fair Value Accounting consultation document. The amendments to paragraph 34D ensure that changes in value will go to the profit and loss account. It is intended that the two sets of regulations will be brought together in a single set before they are laid before Parliament.

5.34 The Government will consider extending the use of fair value accounting to other categories of asset as and when any new IAS in this area are adopted.

Schedule 3 to the draft regulations (Regulation 10(2))

5.35 This amends Schedule 8 to the 1985 Act. Schedule 8 contains the requirements on the form and content of the individual accounts of small companies, as defined in section 247 of the 1985 Act. It is a simplified version of Schedule 4, reflecting the fact that, under the Fourth Directive, small companies are entitled to produce simplified accounts for their shareholders.

5.36 The amendments are identical to those made to Schedule 4 by Regulation 10(1) and Schedule 2.

5.37 It is no longer proposed to exempt small companies from the new requirement (in paragraph 2(3)) to disclose the aggregate amount of dividends proposed in the notes to the accounts. In response to the original consultation on the dividends amendment, the majority of respondents felt that small companies should not be exempt from this. It was argued that the amount of proposed dividends could have a significant impact on the finances of small companies and should therefore be disclosed. The burden of giving this disclosure was considered to be minimal.

Schedule 4 to the draft regulations (Regulation 10(3))

5.38 This amends Schedule 8A to the 1985 Act. Schedule 8A contains the requirements on the form and content of the abbreviated accounts that small companies are currently entitled to lodge with Companies House.

5.39 The amendment in paragraph 2 is identical to that made to Schedule 4 by paragraph 4 of Schedule 2.

Schedule 5 to the draft regulations (Regulation 10(4))

5.40 This amends Schedule 9 to the 1985 Act. Schedule 9 contains the special accounting provisions for banking companies and groups.

5.41 The amendments are identical in substance to those made to Schedule 4 by Schedule 2.

Schedule 6 to the draft regulations (Regulation 10(5))

5.42 This amends Schedule 9A to the 1985 Act. Schedule 9A contains the requirements on the form and content of the accounts of insurance companies and groups.

5.43 The amendments are identical in substance to those made to Schedule 4 by Schedule 2.

Schedule 7 to the draft Regulations (Regulation 11)

5.44 This makes the necessary minor and consequential amendments to the 1985 Act as a result of the amendments in Part 3 of the draft regulations and the attendant schedules.

10. Do you have any comments or suggestions on the drafting of the Regulations on companies at Annex D?

SECTION 6

Proposal for building societies – Detail

The Draft Statutory Instruments for Building Societies

6.1 This section acts as a detailed explanatory note to the draft statutory instruments, explaining the purpose and intention of each provision of each instrument. The implementing provisions are spread over two statutory instruments: the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004 and the Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2004

The Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004

6.2 The Order for amendments to the 1986 Act is divided into four parts. Part 1 (Article 1) is introductory. Part 2 (Article 2) covers amendments to sections of the 1986 Act that are necessary to enable building societies to use International Accounting Standards. Part 3 (Articles 3 to 8) covers amendments to sections of the 1986 Act to implement the Modernisation Directive. Part 4 (Article 9) deals with transitional provisions.

6.3 Part 3 (at Article 8) also inserts a Schedule to the Order containing consequential amendments to the Act. This contains a number of minor changes to take account of the use of IAS and to enable the amendments in the whole Order to sit correctly within the Building Societies Act.

Part 1 of the draft Order

Article 1

6.4 Article 1 provides for the Order to come into force on the day after the day on which it is made and that it applies to financial years of building societies starting on or after 1 January 2005.

Part 2 of the draft Order

Article 2

6.5 Previously, one section of the Building Societies Act 1986, section 72, imposed both the obligation to produce individual accounts and the obligation to produce group accounts. This was followed by section 73 on “Contents and

form of annual accounts". Article 2 replaces existing sections 72 and 73 of the 1986 Act with nine new sections. Firstly, sections 72A, 72B, 72C and 72D, which deal with the preparation of individual accounts by societies and secondly, sections 72E, 72F, 72G, 72H and 72I which deal with the preparation of group accounts by societies with subsidiary undertakings.

6.6 This Article gives effect to the Government's policy of permitting building societies to choose whether to use IAS in the preparation of their accounts, even if they are not obliged to do so for their group accounts by the IAS Regulation. Section 72A(2) now permits all building societies to choose whether to prepare their individual accounts in accordance with provisions of the 1986 Act and regulations made under it or with IAS. Section 72E(2) reflects the fact that building societies with listed securities will be required to prepare their consolidated accounts in accordance with IAS. Section 72E(3) provides that building societies without listed securities can choose to prepare their group accounts in accordance with the 1986 Act or with IAS.

6.7 Section 72A(2) is subject to section 72I which provides that building societies shall, in most circumstances, ensure that the individual accounts of the building society and their subsidiaries are prepared using the same financial reporting framework (i.e. either adopted IAS or UK GAAP), unless there are good reasons for not doing so. This requirement is limited to those subsidiaries that have to prepare accounts under Part VII of the Companies Act 1985. However, the individual accounts of a building society with subsidiaries, do not have to be prepared using the same financial reporting framework as those of the subsidiaries, where the building society is required by the IAS Regulation to use IAS for its consolidated accounts, and has chosen to do so for its individual accounts.

6.8 In the interests of consistency and comparability, it is proposed in section 72A(3) and 72E(4) that building societies choosing to prepare their accounts (both individual and group accounts) under IAS, must continue to do so in subsequent years with no option of reversal.

6.9 Sections 72B(1) and 72F(1) set out which documents must be contained in individual Building Societies Act accounts and group Building Societies Act accounts respectively. The requirements have not altered from those previously contained in section 72 of the Act, but they are now split into two sections, one for individual accounts and one for group accounts. These sections also contain the requirement for the accounts to give a true and fair view and what steps the directors of a building society may take to ensure that the accounts do give a true and fair view. The provisions relating to a true and fair view were previously contained in section 73 of the Act.

6.10 Sections 72C and 72G, set out the regulation making powers for prescribing the form and contents of Building Societies Act individual accounts and group accounts respectively. Each of these sections also retains the duty for a building society director, officer or employee to provide the

information necessary to enable the society to comply with its obligations under the regulations to disclose information about financial interests of or payments to its officers and employees.

6.11 To aid users of accounts, it is proposed in section 72D and 72H that building societies preparing accounts under IAS should be required to disclose this fact in the notes to their accounts.

Part 3 of the draft Order

Articles 3 and 4

6.12 These Articles implement Articles 1.14 and 2.10 of the Modernisation Directive which require more detail to be provided in the annual report and more analysis of risk to be included. The increased detail is required for reports of both individual undertakings and groups of undertakings. Article 3 amends section 75 of the Building Societies Act 1986 in line with the directive requirements. Article 4 inserts a new section 75A into the Act which sets out what the report must contain in terms of review and analysis of the business of the building society and its subsidiaries (if it has subsidiary undertakings). The main change is that the report must now contain a comprehensive analysis of the performance of the business, using key performance indicators where appropriate.

Articles 5, 6 and 7

6.13 These Articles implement Articles 1.15, 1.16 and 1.18 of the Modernisation Directive concerning the audit reports of individual companies, and Article 2.11 concerning the audit reports of groups.

6.14 By specifying matters to be covered in auditors' reports, Article 1.18 of the Modernisation Directive seeks to achieve greater harmonisation and reflect best practice concerning the format and content of audit reports, which currently differ across Member States. Auditing in Britain is in line with best practice, so the amendments required are relatively minor. One of the more significant changes is that, in future, the auditors will need to identify the financial reporting framework applied in the preparation of the accounts.

6.15 Article 5 amends section 78 of the Building Societies Act 1986 to include new requirements for the contents of the auditor's report.

6.16 Article 6 inserts a new section 78A into the Act which is equivalent to the existing section 236 in the Companies Act 1985, in order to implement Article 1.18 of the Directive. This provision requires auditor's reports to be signed and dated by the auditor.

6.17 Article 7 inserts a new section 81A into the Act. This provision is equivalent to one already in the Companies Act 1985 (section 240). It implements Article 1.16 of the Directive and an existing provision of the 4th Accounts Directive which is now applied to building societies. New section 81A requires a building society to include the full auditors' report whenever it publishes its statutory accounts. In addition (in line with the Directive) it requires disclosure, whenever non-statutory accounts are published, of whether the auditors have drawn attention in their report to any matter by way of emphasis, without qualifying the audit report, as well as whether the audit report was qualified or unqualified.

Articles 8 and 9

6.18 Article 8 gives effect to the Schedule to this Order that contains consequential amendments to the Act, made as a result of changes in this Order. Article 9 contains transitional provisions which ensure that existing regulations made under sections 72 and 73 (e.g. The Building Societies (Accounts and Related Provisions) Regulations 1998) continue to have effect and tie in with the newly amended sections of the 1986 Act.

Consequential amendments to the 1986 Act

6.19 The Schedule to the Order contains a number of consequential amendments to take account of the use of IAS and the amendments to the Act to implement the Modernisation Directive. These are minor and self-explanatory apart from the following amendments.

Paragraph 1

6.20 This paragraph amends section 6 of the 1986 Act to allow for the fact that some building societies will now prepare their accounts in accordance with IAS rather than with regulations made under the 1986 Act. The definition of "X" in subsection 2 refers to "liquid assets" and "fixed assets". This terminology is not used in the IAS balance sheet format which instead refers to "current assets" and "non-current assets". The amendment therefore includes the IAS terminology as an alternative.

Paragraph 4

6.21 This paragraph re-enacts the existing disclosure requirements regarding particulars of staff in paragraph 3 of Schedule 5 to the Building Societies (Accounts and Related Provisions) Regulations 1998¹⁵. It is being removed from those regulations and inserted as section 72J in Part VIII of the 1986 Act because these disclosures will also have to be given by a building society preparing accounts in accordance with adopted IAS.

¹⁵ S.I. 1998/504

The Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2004

6.22 These Regulations amend the Building Societies (Accounts and Related Provisions) 1998 (the “principal Regulations”) and deal mainly with implementation of the Modernisation Directive. All the provisions in the main body of the Regulations are implementing changes required by that Directive. There is also a Schedule to the Regulations containing consequential amendments. Some of these consequential amendments are necessary due to amendment of the Building Societies Act 1986 by the Order discussed above. The significant amendments made by these Regulations are discussed below.

Regulation 1

6.23 This provides for the Regulations to come into force on 31 December 2004 and to apply to financial years starting on or after 1 January 2005.

Regulation 2

6.24 This implements Article 2.6 of the Modernisation Directive. It deletes a provision that allowed for an exemption from the requirement to produce consolidated accounts. An undertaking could previously be excluded from the consolidated accounts if its business was so different from that of other undertakings in the group that it would be impossible to give a true and fair view of the group accounts if that undertaking were included. A subsidiary undertaking can no longer be excluded on those grounds.

Regulation 3

6.25 This inserts a provision into the principal Regulations permitting building societies to publish their accounts in ECUs as well as in the currency in which they were drawn up, in line with the requirements of Article 3.1 of the Modernisation Directive. Companies are already permitted to publish their accounts in this alternative currency (see section 242B Companies Act 1985). Now that the Directive requires the same flexibility for financial institutions, this provision, which mirrors section 242B, permits building societies to do the same.

Regulation 4

6.26 This implements Article 3.2 of the Modernisation Directive by altering the title in the layout of the balance sheet so that it no longer refers to “provisions for liabilities and charges” but to “provisions for liabilities”.

Regulation 5

6.27 This implements Article 1.9 of the Directive which removes the requirement to take into account all *foreseeable* liabilities and *potential* losses. The amendment to paragraph 4 of Schedule 7 to the principal Regulations means that the accounts need only include actual liabilities from now on.

Regulation 6

6.28 This implements Article 1.2 of the Modernisation Directive which gives Member States an option. Member States may permit or require the presentation of amounts in the accounts to have regard to the substance of the reported transaction. The proposed new paragraph 20A in Schedule 7 to the principal Regulations requires directors to have regard to the substance of the reported transaction in accordance with generally accepted accounting principles.

6.29 This is a key element in the convergence of UK accounting standards to IAS in the area of financial instruments. It will permit compliance with IAS 32. The Government proposes to implement this as a requirement rather than a permission so that accounts must reflect the substance of the transaction. It is important that formats do not create excessive rigidity and become an obstacle to presenting items in the most meaningful way.

Regulation 7

6.30 This provision inserts new paragraphs into Schedule 7 of the principal Regulations and implements the Member State option in Article 1.12 of the Modernisation Directive. The Fair Value Directive amends the Accounting Directives to permit certain financial instruments to be recorded at fair value in accordance with IAS 39. To deal with future developments, the Modernisation Directive gives Member States the option to extend use of fair value accounting to other asset categories, and to restrict its use to consolidated accounts.

6.31 IAS on investment property (IAS 40 Investment Property) and living animals and plants (IAS 41 Agriculture) have been adopted pursuant to the IAS Regulation. Therefore, the Government has decided to permit these categories of assets to be fair valued in both individual and consolidated accounts. This will facilitate convergence with IAS, and the optional approach is in line with the proposed policy on fair value accounting for financial instruments.

6.32 Article 7 of the Regulations implements this policy, and sets out certain rules for the use of fair value in these circumstances. These amendments should therefore be looked at in the context of the draft regulations in the consultation document on Fair Value Accounting for building societies

(September 2003). It is intended that the fair value accounting regulations will be laid before Parliament close to when these regulations are laid.

6.33 The Government will consider extending the use of fair value accounting to other categories of assets as and when any new IAS in this area are adopted.

Regulation 8

6.34 This implements Article 1.7 of the Modernisation Directive by amending the definition of “provisions for liabilities and charges” in the principal Regulations, so that it sets out the liabilities which ‘provisions’ are intended to cover.

Regulation 9

6.35 This regulation brings the Schedule making minor and consequential amendments to the principal Regulations into effect. As these amendments are merely updating cross-references they are not discussed individually.

11. Do you have any comments or suggestions on the drafting of the Order and Regulations on building societies at Annex E?

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I

(Acts whose publication is obligatory)

**REGULATION (EC) No 1606/2002 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
of 19 July 2002
on the application of international accounting standards**

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 95(1) thereof,

Having regard to the proposal from the Commission ⁽¹⁾,

Having regard to the opinion of the Economic and Social Committee ⁽²⁾,

Acting in accordance with the procedure laid down in Article 251 of the Treaty ⁽³⁾,

Whereas:

- (1) The Lisbon European Council of 23 and 24 March 2000 emphasised the need to accelerate completion of the internal market for financial services, set the deadline of 2005 to implement the Commission's Financial Services Action Plan and urged that steps be taken to enhance the comparability of financial statements prepared by publicly traded companies.
- (2) In order to contribute to a better functioning of the internal market, publicly traded companies must be required to apply a single set of high quality international accounting standards for the preparation of their consolidated financial statements. Furthermore, it is important that the financial reporting standards applied by Community companies participating in financial markets are accepted internationally and are truly global standards. This implies an increasing convergence of accounting standards currently used internationally with the ultimate objective of achieving a single set of global accounting standards.
- (3) Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies ⁽⁴⁾,

Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts ⁽⁵⁾, Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions ⁽⁶⁾ and Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance companies ⁽⁷⁾ are also addressed to publicly traded Community companies. The reporting requirements set out in these Directives cannot ensure the high level of transparency and comparability of financial reporting from all publicly traded Community companies which is a necessary condition for building an integrated capital market which operates effectively, smoothly and efficiently. It is therefore necessary to supplement the legal framework applicable to publicly traded companies.

- (4) This Regulation aims at contributing to the efficient and cost-effective functioning of the capital market. The protection of investors and the maintenance of confidence in the financial markets is also an important aspect of the completion of the internal market in this area. This Regulation reinforces the freedom of movement of capital in the internal market and helps to enable Community companies to compete on an equal footing for financial resources available in the Community capital markets, as well as in world capital markets.
- (5) It is important for the competitiveness of Community capital markets to achieve convergence of the standards used in Europe for preparing financial statements, with international accounting standards that can be used globally, for cross-border transactions or listing anywhere in the world.
- (6) On 13 June 2000, the Commission published its Communication on 'EU Financial Reporting Strategy: the way forward' in which it was proposed that all publicly traded Community companies prepare their consolidated

⁽¹⁾ OJ C 154 E, 29.5.2001, p. 285.

⁽²⁾ OJ C 260, 17.9.2001, p. 86.

⁽³⁾ Opinion of the European Parliament of 12 March 2002 (not yet published in the Official Journal) and Decision of the Council of 7 June 2002.

⁽⁴⁾ OJ L 222, 14.8.1978, p. 11. Directive as last amended by European Parliament and Council Directive 2001/65/EC (OJ L 283, 27.10.2001, p. 28).

⁽⁵⁾ OJ L 193, 18.7.1983, p. 1. Directive as last amended by European Parliament and Council Directive 2001/65/EC.

⁽⁶⁾ OJ L 372, 31.12.1986, p. 1. Directive as last amended by European Parliament and Council Directive 2001/65/EC.

⁽⁷⁾ OJ L 374, 31.12.1991, p. 7.

financial statements in accordance with one single set of accounting standards, namely International Accounting Standards (IAS), at the latest by 2005.

- (7) International Accounting Standards (IASs) are developed by the International Accounting Standards Committee (IASC), whose purpose is to develop a single set of global accounting standards. Further to the restructuring of the IASC, the new Board on 1 April 2001, as one of its first decisions, renamed the IASC as the International Accounting Standards Board (IASB) and, as far as future international accounting standards are concerned, renamed IAS as International Financial Reporting Standards (IFRS). These standards should, wherever possible and provided that they ensure a high degree of transparency and comparability for financial reporting in the Community, be made obligatory for use by all publicly traded Community companies.
- (8) The measures necessary for the implementation of this Regulation should be adopted in accordance with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission⁽¹⁾ and with due regard to the declaration made by the Commission in the European Parliament on 5 February 2002 concerning the implementation of financial services legislation.
- (9) To adopt an international accounting standard for application in the Community, it is necessary firstly that it meets the basic requirement of the aforementioned Council Directives, that is to say that its application results in a true and fair view of the financial position and performance of an enterprise — this principle being considered in the light of the said Council Directives without implying a strict conformity with each and every provision of those Directives; secondly that, in accordance with the conclusions of the Council of 17 July 2000, it is conducive to the European public good and lastly that it meets basic criteria as to the quality of information required for financial statements to be useful to users.
- (10) An accounting technical committee should provide support and expertise to the Commission in the assessment of international accounting standards.
- (11) The endorsement mechanism should act expeditiously on proposed international accounting standards and also be a means to deliberate, reflect and exchange information on international accounting standards among the main parties concerned, in particular national accounting standard setters, supervisors in the fields of securities, banking and insurance, central banks including the ECB, the accounting profession and users and preparers of

accounts. The mechanism should be a means to foster common understanding of adopted international accounting standards in the Community.

- (12) In accordance with the principle of proportionality, the measures provided for in this Regulation, in requiring that a single set of international accounting standards be applied to publicly traded companies, are necessary to achieve the objective of contributing to the efficient and cost-effective functioning of Community capital markets and thereby to the completion of the internal market.
- (13) In accordance with the same principle, it is necessary, as regards annual accounts, to leave to Member States the option to permit or require publicly traded companies to prepare them in conformity with international accounting standards adopted in accordance with the procedure laid down in this Regulation. Member States may decide as well to extend this permission or this requirement to other companies as regards the preparation of their consolidated accounts and/or their annual accounts.
- (14) In order to facilitate an exchange of views and to allow Member States to coordinate their positions, the Commission should periodically inform the accounting regulatory committee about active projects, discussion papers, point outlines and exposure drafts issued by the IASB and about the consequential technical work of the accounting technical committee. It is also important that the accounting regulatory committee is informed at an early stage if the Commission intends not to propose to adopt an international accounting standard.
- (15) In its deliberations on and in elaborating positions to be taken on documents and papers issued by the IASB in the process of developing international accounting standards (IFRS and SIC-IFRIC), the Commission should take into account the importance of avoiding competitive disadvantages for European companies operating in the global marketplace, and, to the maximum possible extent, the views expressed by the delegations in the Accounting Regulatory Committee. The Commission will be represented in constituent bodies of the IASB.
- (16) A proper and rigorous enforcement regime is key to underpinning investors' confidence in financial markets. Member States, by virtue of Article 10 of the Treaty, are required to take appropriate measures to ensure compliance with international accounting standards. The Commission intends to liaise with Member States, notably through the Committee of European Securities Regulators (CESR), to develop a common approach to enforcement.

⁽¹⁾ OJ L 184, 17.7.1999, p. 23.

- (17) Further, it is necessary to allow Member States to defer the application of certain provisions until 2007 for those companies publicly traded both in the Community and on a regulated third-country market which are already applying another set of internationally accepted standards as the primary basis for their consolidated accounts as well as for companies which have only publicly traded debt securities. It is nonetheless crucial that by 2007 at the latest a single set of global international accounting standards, the IAS, apply to all Community companies publicly traded on a Community regulated market.
- (18) In order to allow Member States and companies to carry out the necessary adaptations to make the application of international accounting standards possible, it is necessary to apply certain provisions only in 2005. Appropriate provisions should be put in place for the first-time application of IAS by companies as a result of the entry into force of the present regulation. Such provisions should be drawn up at international level in order to ensure international recognition of the solutions adopted,

HAVE ADOPTED THIS REGULATION:

Article 1

Aim

This Regulation has as its objective the adoption and use of international accounting standards in the Community with a view to harmonising the financial information presented by the companies referred to in Article 4 in order to ensure a high degree of transparency and comparability of financial statements and hence an efficient functioning of the Community capital market and of the Internal Market.

Article 2

Definitions

For the purpose of this Regulation, 'international accounting standards' shall mean International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and related Interpretations (SIC-IFRIC interpretations), subsequent amendments to those standards and related interpretations, future standards and related interpretations issued or adopted by the International Accounting Standards Board (IASB).

Article 3

Adoption and use of international accounting standards

1. In accordance with the procedure laid down in Article 6(2), the Commission shall decide on the applicability within the Community of international accounting standards.
2. The international accounting standards can only be adopted if:
 - they are not contrary to the principle set out in Article 2(3) of Directive 78/660/EEC and in Article 16(3) of Directive

83/349/EEC and are conducive to the European public good and,

- they meet the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

3. At the latest by 31 December 2002, the Commission shall, in accordance with the procedure laid down in Article 6(2), decide on the applicability within the Community of the international accounting standards in existence upon entry into force of this Regulation.

4. Adopted international accounting standards shall be published in full in each of the official languages of the Community, as a Commission Regulation, in the *Official Journal of the European Communities*.

Article 4

Consolidated accounts of publicly traded companies

For each financial year starting on or after 1 January 2005, companies governed by the law of a Member State shall prepare their consolidated accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) if, at their balance sheet date, their securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field ⁽¹⁾.

Article 5

Options in respect of annual accounts and of non publicly-traded companies

Member States may permit or require:

- (a) the companies referred to in Article 4 to prepare their annual accounts,
- (b) companies other than those referred to in Article 4 to prepare their consolidated accounts and/or their annual accounts,

in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2).

Article 6

Committee procedure

1. The Commission shall be assisted by an accounting regulatory committee hereinafter referred to as 'the Committee'.
2. Where reference is made to this paragraph, Articles 5 and 7 of Decision 1999/468/EC shall apply, having regard to the provisions of Article 8 thereof.

⁽¹⁾ OJ L 141, 11.6.1993, p. 27. Directive as last amended by European Parliament and Council Directive 2000/64/EC (OJ L 290, 17.11.2000, p. 27).

The period laid down in Article 5(6) of Decision 1999/468/EC shall be set at three months.

3. The Committee shall adopt its rules of procedure.

Article 7

Reporting and coordination

1. The Commission shall liaise on a regular basis with the Committee about the status of active IASB projects and any related documents issued by the IASB in order to coordinate positions and to facilitate discussions concerning the adoption of standards that might result from these projects and documents.

2. The Commission shall duly report to the Committee in a timely manner if it intends not to propose the adoption of a standard.

Article 8

Notification

Where Member States take measures by virtue of Article 5, they shall immediately communicate these to the Commission and to other Member States.

Article 9

Transitional provisions

By way of derogation from Article 4, Member States may provide that the requirements of Article 4 shall only apply for

each financial year starting on or after January 2007 to those companies:

- (a) whose debt securities only are admitted on a regulated market of any Member State within the meaning of Article 1(13) of Directive 93/22/EEC; or
- (b) whose securities are admitted to public trading in a non-member State and which, for that purpose, have been using internationally accepted standards since a financial year that started prior to the publication of this Regulation in the *Official Journal of the European Communities*.

Article 10

Information and review

The Commission shall review the operation of this Regulation and report thereon to the European Parliament and to the Council by 1 July 2007 at the latest.

Article 11

Entry into force

This Regulation shall enter into force on the third day following that of its publication in the *Official Journal of the European Communities*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 19 July 2002.

For the European Parliament

The President

P. COX

For the Council

The President

T. PEDERSEN

List of Regulated Markets

17.02.2004 List of Regulated Markets under Article 16 of the Investment Services Directive (ISD) (Council Directive 93/22/EEC)

Country	Title of Reg. Market	Operating entity	Competent authority for designation and oversight of market
Austria	1. Amtlicher Handel (official market) 2. Geregelter Freiverkehr (semi-official market) 3. Dritter Markt (third market)	Wiener Börse AG (1-3)	Finanzmarktaufsichtsbehörde
Belgium	1. Bourse de valeurs mobilières d'Euronext Brussels: ■ Le premier marché (official market) ■ Le second marché ■ Le nouveau marché ■ le marché trading facilities 2. Le Marché des Instruments derives d'Euronext Bruxelles 3. Le marché secondaire hors bourse des obligations linéaires, des titres scindés et des certificats de trésorerie 4. Nasdaq Europe	1. Euronext Brussel SA 2. Euronext Brussels SA 3. Fonds des rentes 4. Nasdaq SA	1. Bourse: Législateur = Ministre des Finances; Autorité de Marché = Autorité de Marché d'Euronext Bruxelles. 2. Marché des Instruments derives Ministre des Finances sur avis de la CBF. Autorité de Marché = Autorité de Marché d'Euronext Bruxelles. 3. Ministre des Finances sur proposition du Comité des fonds des rentes. 4. Nasdaq Europe: Ministre des Finances sur avis de la CBF. Autorité de Marché = Autorité de Marché de Nasdaq Europe.
Denmark	1. Københavns Fondsbørs ■ Equity market; ■ Bond market; ■ Derivatives market 2. XtraMarket – Authorised marketplace for unlisted units of investment associations (UCTIS) and Special Purposes Associations 3. Dansk Autoriseret Markedsplads A/S (Danish Authorised Market Place Ltd. (DAMP)) [authorised market place = regular trade in securities admitted for trading but not listed on stock exchange]	1-2. Copenhagen Stock Exchange Ltd. 3. Danish Authorised Market Place Ltd. (DAMP)	Finanstilsynet (Danish financials supervisory authority)

Country	Title of Reg. Market	Operating entity	Competent authority for designation and oversight of market
Finland	<p>1. Arvopaperipörssi (Stock Exchange);</p> <ul style="list-style-type: none"> ■ Päälista (Main List for equity and Debt Instruments); ■ I-, NM-, Pre- ja Meklarien lists (parallel Lists I-, NM-, pre- and Brokers' list for equity and debt instruments); <p>2. Optioyhteisö (Option Corporation). (Derivatives exchange and clearing house).</p>	<p>For both 1 & 2: Helsingin Arvopaperi- ja johdannaispörssi, selvitysyhtiön Oy, (Helsinki Securities and Derivatives Exchange, Clearing House Ltd)</p>	<p>Designation: Ministry of Finance.</p> <p>Oversight:</p> <ul style="list-style-type: none"> ■ Approval of rules: Ministry of Finance; ■ Supervision of compliance: Rahoitustarkastus/Finnish Financial Supervision Authority.
France	<p>1. Bourse de Paris:</p> <ul style="list-style-type: none"> ■ Premier marché (official list); ■ Second marché; ■ Marché des EDR (European Depositary Receipts). <p>2. Nouveau marché</p> <p>3. MATIF</p> <p>4. MONEP</p>	<p>Euronext Paris (1-4)</p>	<p>Proposition de l'Autorité des des marchés financiers (AMF) (cf. article L.4211 du code monétaire et financier).</p> <p>Approbation par le Ministre de l'économie et des finances.</p>
Germany	<p>1. Börse Berlin-Bremen (Amtlicher Handel, Geregelter Markt)</p> <p>2. Düsseldorfer Börse (Amtlicher Handel, Geregelter Markt)</p> <p>3. Frankfurter Wertpapierbörse (Amtlicher Markt, Geregelter Markt)</p> <p>4. Eurex Deutschland</p> <p>5. Hanseatische Wertpapierbörse Hamburg (Amtlicher Markt, Geregelter Markt, Startup market)</p> <p>6. Niedersächsische Börse zu Hannover (Amtlicher Markt, Geregelter Markt)</p> <p>7. Börse München (Amtlicher Markt, Geregelter Markt)</p> <p>8. Baden-Württembergische Wertpapierbörse (Amtlicher Markt, Geregelter Markt)</p>	<p>1. Berliner Börse AG.</p> <p>2. Börse Düsseldorf AG.</p> <p>3 & 4. Deutsche Börse AG.</p> <p>5. BöAG (Börsen AG)</p> <p>6. BöAG (Börsen AG)</p> <p>7. Bayerische Börse AG</p> <p>8. Börse-Stuttgart AG</p>	<p>Börsenaufsichtsbehörden de Länder (stock exchange supervisory authorities of the deferral states) and the Bundesanstalt für Finanzdienstleistungsaufsicht (BAFin).</p> <p>State authorities:</p> <ol style="list-style-type: none"> 1. Senatsverwaltung für Wirtschaft und Technologie, Berlin. 2. Finanzministerium des Landes Nordrhein-Westfalen, Düsseldorf. 3 & 4. Hessisches Ministerium für Wirtschaft, Verkehr und Landesentwicklung, Wiesbaden. 5. Freie und Hansestadt Hamburg, Wirtschaftsbehörde. 6. Niedersächsisches Ministerium für Wirtschaft, Technologie und Verkehr, Hanover. 7. Bayerisches Staatsministerium für Wirtschaft, Verkehr und Technologie, München. 8. Wirtschaftsministerium Baden-Württemberg, Stuttgart.

Country	Title of Reg. Market	Operating entity	Competent authority for designation and oversight of market
Greece	<p>1. Athens Stock Exchange (A.S.E)/Thessaloniki Stock Exchange Centre T.S.E.C.)</p> <ul style="list-style-type: none"> ■ Main Market ■ Parallel Market ■ Parallel Market for Emerging Markets ■ New Market <p>2. Athens Derivatives Exchange (A.D.EX)</p> <p>3. Electronic Secondary Securities Market (HDAT-Bond Market, under the competence and supervision of the Bank of Greece)</p>	<p>1 and 2. Athens Stock Exchange</p> <p>3. Bank of Greece</p>	Capital market Commission
Ireland	<p>Irish Stock Exchange comprising:</p> <ul style="list-style-type: none"> ■ Official List ■ Exploration Securities Market ■ Developing Companies Market ■ ITEQ 	Irish Stock Exchange Ltd.	The Irish Financial Services Regulatory Authority authorises “regulated market” and (with exc. of listing conditions) vets and approves rules for operation of the different segments as prepared by the ISE.
Italy	<p>1. Stock Exchange, divided into the following segments:</p> <ul style="list-style-type: none"> ■ Electronic share market (MTA); ■ Electronic covered warrants market (MCW); ■ After-Hours Market (TAH); ■ Electronic bond and government securities market (MOT); ■ Electronic market for Eurobonds, foreign bonds and asset-backed securities (EuroMOT). <p>2. Mercato Ristretto (second market).</p> <p>3. Derivatives market (DEM).</p> <p>4. Nuovo Mercato (New Market – NM).</p> <p>5. Wholesale Market for Corporate and International Organisations Bonds.</p> <p>6. Wholesale Market for Corporate and International Organisations Bonds.</p>	<p>(1-4) Borsa Italiana S.p.A.</p> <p>(5-6) Società per il Mercato dei Titoli di Stato – MTS S.p.A.:</p>	CONSOB authorises companies which manage markets, and approves For wholesale markets for Government securities, operating company is authorised by Treasury having regard to the opinion of CONSOB and Banca d’Italia.
Luxembourg	Bourse de Luxembourg: Official List	Société de la Bourse de Luxembourg S.A.	Commission de surveillance du Secteur Financier

Country	Title of Reg. Market	Operating entity	Competent authority for designation and oversight of market
Netherlands	<p>1. Euronext Amsterdam Cash Market:</p> <ul style="list-style-type: none"> ■ Official market ■ Domestic market for unlisted securities ■ Euro NM Amsterdam <p>2. Euronext Amsterdam derivatives Market.</p>	Euronext N.V. and Euronext Amsterdam N.V.	Recognition by the Minister of Finance after advice from the Netherlands Authority for the Financial Markets. Supervision by the Netherlands authority for the Financial Markets and The Netherlands Ministry of Finance.
Portugal	<p>1. Mercado de Cotações Oficiais (Official Quotation Market)</p> <p>2. Segundo Mercado (Second Market)</p> <p>3. Novo Mercado (New Market)</p> <p>4. Mercado de Futurose e Opções (Futures and Options Market)</p> <p>5. MEDIP – Mercado Especial de Dívida Pública (Special Market for Public Debt)</p>	<p>Markets 1-4: Euronext Lisboa – Sociedade Gestora de Mercados Regulamentados SA</p> <p>Market 5: MTS Portugal – Sociedade Gestora Mercado Especial Dívida Pública SA</p>	Finance Ministry authorises markets on basis of proposal from Comissão do Mercado de Valores Mobiliários (CMVM) – latter responsible for regulation and oversight of market.
Spain	<p>A. Bolsas de Valores (all comprise first, second and new market segments)</p> <p>1. Bolsa de Valores de Barcelona;</p> <p>2. Bolsa de Valores de Bilbao;</p> <p>3. Bolsa de Valores de Madrid;</p> <p>4. Bolsa de Valores de Valencia.</p> <p>B. Mercados oficiales de Productos Financieros Derivados</p> <p>1. MEFF Renta Fija;</p> <p>2. MEFF Renta Variable.</p> <p>C. Mercados FC&M de Futuros y Opciones sobre Cítricos [commodity derivatives not covered by section B annex ISD: related markets do not fall within ISD definition of “regulated market”]</p> <p>D. AIAF Mercado de Renta Fija.</p> <p>E. Mercado de Deuda Pública en Anotaciones.</p>	<p>A1. Sociedad Rectora de la Bolsa de Valores de Barcelona S.A.</p> <p>A2. Soc. Rectora de la Bolsa de Valores de Bilbao S.A.</p> <p>A3. Soc. Rectora de la Bolsa de Valores de Madrid S.A.</p> <p>A4. Soc. Recotora de la Bolsa de Valores de Valencia S.A.</p> <p>B1. Soc. Rectora de Productos Financieros Derivados de RENTA Fija S.A.</p> <p>B2. Soc. Rectora de Productos Financieros Derivados de Renta Variable S.A.</p> <p>C. (FC&M) Soc. Rectora del Mercado de Futuros y Opciones sobre Criticos SA.</p> <p>D. AIAF Mercado de Renta Fija.</p>	<p>CNMV (Comisión Nacional del Mercado de Valores)</p> <p>Banco de España responsible for market for public debt.</p>

Country	Title of Reg. Market	Operating entity	Competent authority for designation and oversight of market
Sweden	1. Stockholmsbörsen: 2. Nordic Growth Market 3. Aktietorget	1. Stockholmsbörsen Aktiebolag 2. Nordic Growth Market NGM-Aktiebolag. 3. Aktietorget Aktiebolag.	Finansinspektionen (Financial Supervisory Authority)
United Kingdom	1. Domestic Equity Market 2. European Equity Market 3. Gilt Edged and Sterling Bond Market 4. Alternative Investment Market (AIM) 5. International Retail Service 6. International Order Book 7. The London International Financial Futures and Options Exchange (LIFFE) 8. Virt-x 9. EDX	Markets 1-6. London Stock Exchange Ltd. 7. LIFFE Administration and Management. 8. Virt-x Exchange Limited 9. EDX London Limited	Entities operating regulated markets are recognised investment exchanges within the meaning of s285 of the Financial Services Act 2000 and are regulated by the Financial Services Authority (FSA).
Iceland	1. Verðbréfa_ing Íslands hf. (kauphöll Íslands. – official market) 2. Tilboðsmarkaður V_Í (Regulated OTC Market – not official listing)	1. Kauphöll Íslands. 2. Kauphöll Íslands.	Fjármála-eftirlitið (Financial Supervisory Authority)
Norway	Oslo Stock Exchange ■ Equity Market ■ Derivative Market ■ Bonds Market	Oslo Børs ASA	Kredittilsynet (The Banking, Insurance and Securities Commission of Norway)

Modernisation Directive

L 178/16

EN

Official Journal of the European Union

17.7.2003

DIRECTIVE 2003/51/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 18 June 2003

amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 44(1) thereof,

Having regard to the proposal from the Commission ⁽¹⁾,

Having regard to the opinion of the European Economic and Social Committee ⁽²⁾,

Acting in accordance with the procedure laid down in Article 251 of the Treaty ⁽³⁾,

Whereas:

- (1) The Lisbon European Council of 23-24 March 2000 emphasised the need to accelerate completion of the internal market for financial services, set the deadline of 2005 for implementation of the Commission's Financial Services Action Plan and urged that steps be taken to enhance the comparability of financial statements prepared by Community companies whose securities are admitted to trading on a regulated market (hereinafter: listed companies).
- (2) On 13 June 2000, the Commission published its Communication entitled 'EU Financial Reporting Strategy: The Way Forward' in which it was proposed that all listed companies prepare their consolidated accounts in accordance with one single set of accounting standards, namely International Accounting Standards (IAS), at the latest by 2005.
- (3) Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards ⁽⁴⁾ (hereinafter: the IAS Regulation) introduced the requirement that, from 2005 onwards, all listed companies prepare their consolidated accounts in accordance with IAS adopted for application within the Community. It also provided an option for Member States to permit or require the application of adopted IAS in the preparation of annual accounts and to permit or require the application of adopted IAS by unlisted companies.

- (4) The IAS Regulation provides that, to adopt an international accounting standard for its application in the Community, it is necessary that it meets the basic requirement of the Fourth Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies ⁽⁵⁾ and of the Seventh Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts ⁽⁶⁾, that is to say that its application results in a true and fair view of the financial position and performance of an enterprise — this principle being considered in the light of the said Directives without implying a strict conformity with each and every provision of those Directives.
- (5) As the annual and consolidated accounts of undertakings covered by Directives 78/660/EEC and 83/349/EEC which are not prepared in accordance with the IAS Regulation will continue to have those Directives as the primary source of their Community accounting requirements, it is important that a level playing field exists between Community companies which apply IAS and those which do not.
- (6) For the purposes both of the adoption of IAS and the application of Directives 78/660/EEC and 83/349/EEC, it is desirable that those Directives reflect developments in international accounting. In this respect, the Communication of the Commission entitled 'Accounting Harmonisation: A New Strategy vis-à-vis International Harmonisation' called for the European Union to work to maintain consistency between Community Accounting Directives and developments in international accounting standard setting, in particular within the International Accounting Standards Committee (IASC).
- (7) Member States should be able to modify the presentation of the profit and loss account and balance sheet in accordance with international developments, as expressed through standards issued by the International Accounting Standards Board (IASB).
- (8) Member States should be able to permit or require the application of revaluations and of fair value in accordance with international developments, as expressed through standards issued by the IASB.

⁽¹⁾ OJ C 227 E, 24.9.2002, p. 336.

⁽²⁾ OJ C 85, 8.4.2003, p. 140.

⁽³⁾ Opinion of the European Parliament of 14 January 2003 (not yet published in the Official Journal), and Council Decision of 6 May 2003.

⁽⁴⁾ OJ L 243, 11.9.2002, p. 1.

⁽⁵⁾ OJ L 222, 14.8.1978, p. 11. Directive as last amended by Directive 2001/65/EC of the European Parliament and of the Council (OJ L 283, 27.10.2001, p. 28).

⁽⁶⁾ OJ L 193, 18.7.1983, p. 1. Directive as last amended by Directive 2001/65/EC.

- (9) The annual report and the consolidated annual report are important elements of financial reporting. Enhancement, in line with current best practice, of the existing requirement for these to present a fair review of the development of the business and of its position, in a manner consistent with the size and complexity of the business, is necessary to promote greater consistency and give additional guidance concerning the information a 'fair review' is expected to contain. The information should not be restricted to the financial aspects of the company's business. It is expected that, where appropriate, this should lead to an analysis of environmental and social aspects necessary for an understanding of the company's development, performance or position. This is consistent also with Commission Recommendation 2001/453/EC of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies ⁽¹⁾. However, taking into account the evolving nature of this area of financial reporting and having regard to the potential burden placed on undertakings below certain sizes, Member States may choose to waive the obligation to provide non-financial information in the case of the annual report of such undertakings.
- (10) Differences in the preparation and presentation of the audit report reduce comparability and detract from the user's understanding of this vital aspect of financial reporting. Increased consistency should be achieved by amendments, consistent with current international best practice, to the specific requirements concerning the format and content of an audit report. The fundamental requirement that an audit opinion states whether the annual or consolidated accounts give a true and fair view in accordance with the relevant financial reporting framework does not represent a restriction of the scope of that opinion but clarifies the context in which it is expressed.
- (11) Directives 78/660/EEC and 83/349/EEC should accordingly be amended. Furthermore, it is also necessary to amend Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions ⁽²⁾.
- (12) The IASB is developing and refining the accounting standards applicable to insurance activities.
- (13) Insurance undertakings should also be allowed to use fair-value accounting as expressed through appropriate standards issued by the IASB.
- (14) Consequently Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings ⁽³⁾ should be amended.
- (15) These amendments will remove all inconsistencies between Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the one hand and IAS in existence at 1 May 2002, on the other,

HAVE ADOPTED THIS DIRECTIVE:

Article 1

Directive 78/660/EEC is hereby amended as follows:

1. in Article 2(1) the following subparagraph shall be added:
'Member States may permit or require the inclusion of other statements in the annual accounts in addition to the documents referred to in the first subparagraph.'
2. in Article 4, the following paragraph shall be added:
'6. Member States may permit or require the presentation of amounts within items in the profit and loss account and balance sheet to have regard to the substance of the reported transaction or arrangement. Such permission or requirement may be restricted to certain classes of company and/or to consolidated accounts as defined in the Seventh Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts (*).'

(*) OJ L 193, 18.7.1983, p. 1. Directive as last amended by Directive 2001/65/EC of the European Parliament and of the Council (OJ L 283, 27.10.2001, p. 28).';
3. in Article 8 the following paragraph shall be added:
'Member States may permit or require companies to adopt the presentation of the balance sheet set out in Article 10a as an alternative to the layouts otherwise prescribed or permitted.'
4. in Article 9, under 'Liabilities', in point B, the title 'Provisions for liabilities and charges' shall be replaced by 'Provisions';
5. in Article 10, point J, the title 'Provisions for liabilities and charges' shall be replaced by 'Provisions';
6. the following Article shall be inserted:

'Article 10a

Instead of the presentation of balance sheet items in accordance with Articles 9 and 10, Member States may permit or require companies, or certain classes of company, to present those items on the basis of a distinction between current and non-current items provided that the information given is at least equivalent to that otherwise required by Articles 9 and 10.'

⁽¹⁾ OJ L 156, 13.6.2001, p. 33.

⁽²⁾ OJ L 372, 31.12.1986, p. 1. Directive as last amended by Directive 2001/65/EC.

⁽³⁾ OJ L 374, 31.12.1991, p. 7.

7. Article 20 shall be amended as follows:

(a) Paragraph 1 shall be replaced by the following:

'1. Provisions are intended to cover liabilities the nature of which is clearly defined and which at the date of the balance sheet are either likely to be incurred, or certain to be incurred but uncertain as to amount or as to the date on which they will arise.';

(b) Paragraph 3 shall be replaced by the following:

'3. Provisions may not be used to adjust the values of assets.';

8. in Article 22, the following paragraph shall be added:

'By way of derogation from Article 2(1), Member States may permit or require all companies, or any classes of company, to present a statement of their performance instead of the presentation of profit and loss items in accordance with Articles 23 to 26, provided that the information given is at least equivalent to that otherwise required by those Articles.';

9. Article 31 shall be amended as follows:

(a) in paragraph 1(c), point (bb) shall be replaced by the following:

'(bb) account must be taken of all liabilities arising in the course of the financial year concerned or of a previous one, even if such liabilities become apparent only between the date of the balance sheet and the date on which it is drawn up,';

(b) the following paragraph shall be inserted:

'(1a) In addition to those amounts recorded pursuant to paragraph (1)(c)(bb), Member States may permit or require account to be taken of all foreseeable liabilities and potential losses arising in the course of the financial year concerned or of a previous one, even if such liabilities or losses become apparent only between the date of the balance sheet and the date on which it is drawn up.';

10. in Article 33(1), point (c) shall be replaced by the following:

'(c) revaluation of fixed assets';

11. in Article 42, the first paragraph shall be replaced by the following:

'Provisions may not exceed in amount the sums which are necessary.';

12. the following Articles shall be inserted:

'Article 42e

By way of derogation from Article 32, Member States may permit or require in respect of all companies or any classes of company the valuation of specified categories of assets other than financial instruments at amounts determined by reference to fair value.

Such permission or requirement may be restricted to consolidated accounts as defined in Directive 83/349/EEC.

Article 42f

Notwithstanding Article 31(1)(c), Member States may permit or require in respect of all companies or any classes of company that, where an asset is valued in accordance with Article 42e, a change in the value is included in the profit and loss account.';

13. in Article 43(1)(6) the reference to 'Articles 9 and 10' shall be replaced by a reference to 'Articles 9, 10 and 10a';

14. Article 46 shall be amended as follows:

(a) paragraph 1 shall be replaced by the following:

'1. (a) The annual report shall include at least a fair review of the development and performance of the company's business and of its position, together with a description of the principal risks and uncertainties that it faces.

The review shall be a balanced and comprehensive analysis of the development and performance of the company's business and of its position, consistent with the size and complexity of the business;

(b) To the extent necessary for an understanding of the company's development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters;

(c) In providing its analysis, the annual report shall, where appropriate, include references to and additional explanations of amounts reported in the annual accounts.';

(b) the following paragraph shall be added:

'4. Member States may choose to exempt companies covered by Article 27 from the obligation in paragraph 1(b) above in so far as it relates to non-financial information.';

15. in Article 48, the third sentence shall be deleted;

16. in Article 49, the third sentence shall be replaced by the following:

'The report of the person or persons responsible for auditing the annual accounts (hereinafter: the statutory auditors) shall not accompany this publication, but it shall be disclosed whether an unqualified, qualified or adverse audit opinion was expressed, or whether the statutory auditors were unable to express an audit opinion. It shall also be disclosed whether the report of the statutory auditors included a reference to any matters to which the statutory auditors drew attention by way of emphasis without qualifying the audit opinion.';

17. Article 51(1) shall be replaced by the following:

'1. The annual accounts of companies shall be audited by one or more persons approved by Member States to carry out statutory audits on the basis of the Eighth Council Directive 84/253/EEC of 10 April 1984 on the approval of persons responsible for carrying out the statutory audits of accounting documents (*).

The statutory auditors shall also express an opinion concerning the consistency or otherwise of the annual report with the annual accounts for the same financial year.

(*) OJ L 126, 12.5.1984, p. 20.;

18. the following Article shall be inserted:

'Article 51a

1. The report of the statutory auditors shall include:

- (a) an introduction which shall at least identify the annual accounts that are the subject of the statutory audit, together with the financial reporting framework that has been applied in their preparation;
- (b) a description of the scope of the statutory audit which shall at least identify the auditing standards in accordance with which the statutory audit was conducted;
- (c) an audit opinion which shall state clearly the opinion of the statutory auditors as to whether the annual accounts give a true and fair view in accordance with the relevant financial reporting framework and, where appropriate, whether the annual accounts comply with statutory requirements; the audit opinion shall be either unqualified, qualified, an adverse opinion or, if the statutory auditors are unable to express an audit opinion, a disclaimer of opinion;
- (d) a reference to any matters to which the statutory auditors draw attention by way of emphasis without qualifying the audit opinion;
- (e) an opinion concerning the consistency or otherwise of the annual report with the annual accounts for the same financial year.

2. The report shall be signed and dated by the statutory auditors.;

19. Article 53(1) shall be deleted;

20. the following Article shall be inserted:

'Article 53a

Member States shall not make available the exemptions set out in Articles 11, 27, 46, 47 and 51 in the case of companies whose securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field (*).

(*) OJ L 141, 11.6.1993, p. 27. Directive as last amended by Directive 2002/87/EC of the European Parliament and of the Council (OJ L 35, 11.2.2003, p. 1).;

21. in Article 56(1) the reference to 'Articles 9, 10' shall be replaced by a reference to 'Articles 9, 10, 10a';

22. in Article 60, first paragraph, the words 'on the basis of their market value' shall be replaced by 'on the basis of their fair value';

23. in Article 61a, the reference to 'Articles 42a to 42d' shall be replaced by a reference to 'Articles 42a to 42f'.

Article 2

Directive 83/349/EEC is hereby amended as follows:

1. in Article 1, paragraph 2 shall be replaced by the following:

'2. Apart from the cases mentioned in paragraph 1 the Member States may require any undertaking governed by their national law to draw up consolidated accounts and a consolidated annual report if:

- (a) that undertaking (a parent undertaking) has the power to exercise, or actually exercises, dominant influence or control over another undertaking (the subsidiary undertaking); or
- (b) that undertaking (a parent undertaking) and another undertaking (the subsidiary undertaking) are managed on a unified basis by the parent undertaking.;

2. in Article 3(1), the reference to 'Articles 13, 14 and 15' shall be replaced by a reference to 'Articles 13 and 15';

3. Article 6 shall be amended as follows:

(a) paragraph 4 shall be replaced by the following:

'4. This Article shall not apply where one of the undertakings to be consolidated is a company whose securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field (*).

(*) OJ L 141, 11.6.1993, p. 27. Directive as last amended by Directive 2002/87/EC of the European Parliament and of the Council (OJ L 35, 11.2.2003, p. 1).;

(b) paragraph 5 shall be deleted;

4. Article 7 shall be amended as follows:

- (a) in paragraph 1(b), the second sentence shall be deleted;
- (b) in paragraph 2(a), the reference to 'Articles 13, 14 and 15' shall be replaced by a reference to 'Articles 13 and 15';
- (c) paragraph 3 shall be replaced by the following:

'3. This Article shall not apply to companies whose securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Directive 93/22/EEC.;

5. in Article 11(1)(a) the reference to 'Articles 13, 14 and 15' shall be replaced by a reference to 'Articles 13 and 15';

6. Article 14 shall be deleted;

7. in Article 16(1) the following subparagraph shall be added:

'Member States may permit or require the inclusion of other statements in the consolidated accounts in addition to the documents referred to in the first subparagraph.');

8. in Article 17(1) the reference to 'Articles 3 to 10' shall be replaced by a reference to 'Articles 3 to 10a';

9. Article 34 shall be amended as follows:

(a) in point (2)(b) the terms 'Articles 13 and 14 and, without prejudice to Article 14(3),' shall be replaced by a reference to 'Article 13 and';

(b) in point (5) the words 'and those excluded pursuant to Article 14' shall be deleted;

10. Article 36 shall be amended as follows:

(a) paragraph 1 shall be replaced by the following:

'1. The consolidated annual report shall include at least a fair review of the development and performance of the business and of the position of the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The review shall be a balanced and comprehensive analysis of the development and performance of the business and of the position of the undertakings included in the consolidation taken as a whole, consistent with the size and complexity of the business. To the extent necessary for an understanding of such development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters.

In providing its analysis, the consolidated annual report shall, where appropriate, provide references to and additional explanations of amounts reported in the consolidated accounts.');

(b) The following paragraph shall be added:

'3. Where a consolidated annual report is required in addition to an annual report, the two reports may be presented as a single report. In preparing such a single report, it may be appropriate to give greater emphasis to those matters which are significant to the undertakings included in the consolidation taken as a whole.');

11. Article 37 shall be replaced by the following:

'Article 37

1. The consolidated accounts of companies shall be audited by one or more persons approved by the Member State whose laws govern the parent undertaking to carry

out statutory audits on the basis of the Eighth Council Directive 84/253/EEC of 10 April 1984 on the approval of persons responsible for carrying out the statutory audits of accounting documents (*).

The person or persons responsible for auditing the consolidated accounts (hereinafter: the statutory auditors) shall also express an opinion concerning the consistency or otherwise of the consolidated annual report with the consolidated accounts for the same financial year.

2. The report of the statutory auditors shall include:

(a) an introduction which shall at least identify the consolidated accounts which are the subject of the statutory audit, together with the financial reporting framework that has been applied in their preparation;

(b) a description of the scope of the statutory audit which shall at least identify the auditing standards in accordance with which the statutory audit was conducted;

(c) an audit opinion which shall state clearly the opinion of the statutory auditors as to whether the consolidated accounts give a true and fair view in accordance with the relevant financial reporting framework and, where appropriate, whether the consolidated accounts comply with statutory requirements; the audit opinion shall be either unqualified, qualified, an adverse opinion or, if the statutory auditors are unable to express an audit opinion, a disclaimer of opinion;

(d) a reference to any matters to which the statutory auditors draw attention by way of emphasis without qualifying the audit opinion;

(e) an opinion concerning the consistency or otherwise of the consolidated annual report with the consolidated accounts for the same financial year.

3. The report shall be signed and dated by the statutory auditors.

4. Where the annual accounts of the parent undertaking are attached to the consolidated accounts, the report of the statutory auditors required by this Article may be combined with any report of the statutory auditors on the annual accounts of the parent undertaking required by Article 51 of Directive 78/660/EEC.

(*) OJ L 126, 12.5.1984, p. 20.;

12. in Article 38, the following paragraph shall be added:

'7. Paragraphs 2 and 3 shall not be applied in respect of companies whose securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Directive 93/22/EEC.'

Article 3

Directive 86/635/EEC is hereby amended as follows:

1. in Article 1, paragraphs 1 and 2 shall be replaced by the following:

'1. Articles 2, 3, 4(1), (3) to (6), Articles 6, 7, 13, 14, 15(3) and (4), Articles 16 to 21, 29 to 35, 37 to 41, 42 first sentence, 42a to 42f, 45(1), 46(1) and (2), Articles 48 to 50, 50a, 51(1) and 51a, 56 to 59, 61 and 61a of Directive 78/660/EEC shall apply to the institutions mentioned in Article 2 of this Directive, except where this Directive provides otherwise. However, Articles 35(3), 36, 37 and 39(1) to (4) of this Directive shall not apply with respect to assets and liabilities that are valued in accordance with Section 7a of Directive 78/660/EEC.

2. Where reference is made in Directives 78/660/EEC and 83/349/EEC to Articles 9, 10 and 10a (balance sheet) or to Articles 22 to 26 (profit and loss account) of Directive 78/660/EEC, such references shall be deemed to be references to Articles 4 and 4a (balance sheet) or to Articles 26, 27 and 28 (profit and loss account) of this Directive.'

2. Article 4 shall be amended as follows:

- (a) the first sentence shall be replaced by the following:

'The Member States shall prescribe the following layout for the balance sheet. As an alternative, Member States may permit or require credit institutions to adopt the presentation of the balance sheet set out in Article 4a.'

- (b) under 'Liabilities', in point 6, the title 'Provisions for liabilities and charges' shall be replaced by 'Provisions';

3. the following Article shall be inserted:

'Article 4a

Instead of the presentation of balance sheet items in accordance with Article 4, Member States may permit or require credit institutions, or certain classes of credit institution, to present those items classified by their nature and in order of their relative liquidity provided that the information given is at least equivalent to that otherwise required by Article 4.;

4. in Article 26, the following paragraph shall be added:

'By way of derogation from Article 2(1) of Directive 78/660/EEC, Member States may permit or require all credit institutions, or any classes of credit institution, to present a statement of their performance instead of the presentation of profit and loss items in accordance with Articles 27 or 28, provided that the information given is at least equivalent to that otherwise required by those Articles.'

5. Article 43(2)(f) shall be deleted.

Article 4

Directive 91/674/EEC is hereby amended as follows:

1. in Article 1, paragraphs 1 and 2 shall be replaced by the following:

'1. Articles 2, 3, 4(1), (3) to (6), 6, 7, 13, 14, 15(3) and (4), 16 to 21, 29 to 35, 37 to 41, 42, 42a to 42f, 43(1), points 1 to 7 and 9 to 14, 45(1), 46(1) and (2), 48 to 50, 50a, 51(1), 51a, 56 to 59, 61 and 61a of Directive 78/660/EEC shall apply to the undertakings mentioned in Article 2 of this Directive, except where this Directive provides otherwise. Articles 46, 47, 48, 51 and 53 of this Directive shall not apply in respect of assets and liabilities that are valued in accordance with Section 7a of Directive 78/660/EEC.

2. Where reference is made in Directives 78/660/EEC and 83/349/EEC to Articles 9, 10 and 10a (balance sheet) or to Articles 22 to 26 (profit and loss account) of Directive 78/660/EEC, such references shall be deemed to be references to Article 6 (balance sheet) or to Article 34 (profit and loss account) of this Directive as appropriate.'

2. Article 4 shall be replaced by the following:

'Article 4

1. This Directive shall apply to the association of underwriters known as Lloyd's. For the purpose of this Directive both Lloyd's and Lloyd's syndicates shall be deemed to be insurance undertakings.

2. By way of derogation from Article 65(1), Lloyd's shall prepare aggregate accounts instead of consolidated accounts required by Directive 83/349/EEC. Aggregate accounts shall be prepared by cumulation of all syndicate accounts.'

3. in Article 6, under 'Liabilities', in point E, the title 'Provisions for other risks and charges' shall be replaced by 'Other provisions';

4. Article 46 shall be amended as follows:

- (a) in paragraph 5, the following sentence shall be added:

'Member States may permit derogations from this requirement.'

- (b) paragraph 6 shall be replaced by the following:

'6. The method(s) applied to each investment item shall be stated in the notes on the accounts, together with the amounts so determined.'

5. the following Article shall be inserted:

'Article 46a

1. Where assets and liabilities are valued in accordance with Section 7a of Directive 78/660/EEC, paragraphs 2 to 6 of this Article shall apply.

2. The investments shown as assets under D shall be shown at their fair value.

3. Where investments are shown at their purchase price, their fair value shall be disclosed in the notes on the accounts.

4. Where investments are shown at their fair value, their purchase price shall be disclosed in the notes on the accounts.

5. The same valuation method shall be applied to all investments included in any item denoted by an arabic numeral or shown as assets under C(I). Member States may permit derogations from this requirement.

6. The method(s) applied to each investment item shall be stated in the notes on the accounts, together with the amounts so determined.;

6. the Annex shall be deleted.

Article 5

Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 1 January 2005 at the latest. They shall forthwith inform the Commission thereof.

When Member States adopt these measures, they shall contain a reference to this Directive or shall be accompanied by such a reference on the occasion of their official publication. The methods of making such reference shall be laid down by the Member States.

Article 6

This Directive shall enter into force on the day of its publication in the *Official Journal of the European Union*.

Article 7

This Directive is addressed to the Member States.

Done at Luxembourg, 18 June 2003.

For the European Parliament

The President

P. COX

For the Council

The President

G. DRYS

Draft Statutory Instrument for Companies under the Companies Act 1985

2004 No.

COMPANIES

The Companies Act 1985 (International Accounting Standards and Other
Accounting Amendments) Regulations 2004

Made.....2004

Coming into force2004

[CONSULTATION DRAFT]

The Secretary of State, in exercise of the powers conferred on her by section 257 of the Companies Act 1985¹⁶ and of all other powers enabling her in that behalf, hereby makes the following Regulations of which a draft has been laid before Parliament in accordance with section 257(2) of that Act and approved by resolution of each House of Parliament:

PART I

General

Citation, commencement and interpretation

1. (1) These Regulations may be cited as the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004.

(2) These Regulations come into force on the day after the day on which they are made, and have effect as respects companies' financial years which begin on or after 1st January 2005.

(3) In paragraph (2), the reference to financial years beginning on or after 1st January 2005 includes financial years which would have so begun but for the exercise (on or after the date of making of these Regulations) of the power conferred by section 223 of the 1985 Act (calculation of company's financial year)¹⁷.

(4) In these Regulations, "the 1985 Act" means the Companies Act 1985.

¹⁶ 1985 c.6; section 257 was substituted by section 20 of the Companies Act 1989 (1989 c.40).

¹⁷ Section 223 was substituted by section 3 of the Companies Act 1989 (c.40).

PART 2

Accounts prepared in accordance with international accounting standards

Preparation of individual accounts in accordance with IAS Regulation

2. For sections 226 and 227 of the 1985 Act (duty to prepare individual and group accounts)¹⁸ substitute -

226 Duty to prepare individual accounts

(1) The directors of every company must prepare accounts for the company for each of its financial years.

Those accounts are referred to in this Part as the company's "individual accounts".

(2) A company's individual accounts may be prepared -

(a) in accordance with section 226A ("Companies Act individual accounts"), or

(b) in accordance with international accounting standards ("IAS individual accounts").

This subsection is subject to the following provisions of this section and section 227C (consistency of accounts).

(3) A company that is a charity must prepare Companies Act individual accounts.

(4) Where the directors of a company have prepared IAS individual accounts for a financial year, they must prepare all subsequent individual accounts for the company in accordance with international accounting standards.

(5) Subsection (4) does not apply if the company becomes a subsidiary undertaking of another EEA undertaking and that EEA undertaking does not prepare IAS individual accounts.

(6) In this section "EEA undertaking" means an undertaking established under the law of any part of the United Kingdom or the law of any other EEA State.

226A Companies Act individual accounts

(1) Companies Act individual accounts must comprise -

(a) a balance sheet as at the last day of the financial year, and

(b) a profit and loss account.

¹⁸ Section 226 was substituted by section 4(1) of the Companies Act 1989, and section 227 by section 5(1) of that Act.

(2) The balance sheet must give a true and fair view of the state of affairs of the company as at the end of the financial year; and the profit and loss account must give a true and fair view of the profit or loss of the company for the financial year.

(3) Companies Act individual accounts must comply with the provisions of Schedule 4 as to the form and content of the balance sheet and profit and loss account and additional information to be provided by way of notes to the accounts.

(4) Where compliance with the provisions of that Schedule, and the other provisions of this Act as to the matters to be included in a company's individual accounts or in notes to those accounts, would not be sufficient to give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.

(5) If in special circumstances compliance with any of those provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent necessary to give a true and fair view.

(6) Particulars of any such departure, the reasons for it and its effect must be given in a note to the accounts.

226B IAS individual accounts

Where the directors of a company prepare IAS individual accounts, they must state in the notes to those accounts that the accounts have been prepared in accordance with international accounting standards.

227 Duty to prepare group accounts

(1) If at the end of a financial year a company is a parent company the directors, as well as preparing individual accounts for the year, must prepare consolidated accounts for the group for the year.

Those accounts are referred to in this Part as the company's "group accounts".

(2) Certain companies are obliged by Article 4 of the IAS Regulation to prepare their group accounts in accordance with international accounting standards ("IAS group accounts").

(3) The group accounts of other companies may be prepared -

(a) in accordance with section 227A ("Companies Act group accounts"), or

(b) in accordance with international accounting standards ("IAS group accounts").

This subsection is subject to the following provisions of this section and section 227C (consistency of accounts).

(4) A parent company that is a charity must prepare Companies Act group accounts.

(5) Where the directors of a parent company have prepared IAS group accounts for a financial year, they must prepare all subsequent group accounts for the company in accordance with international accounting standards.

(6) Subsection (5) does not apply if the company becomes a subsidiary undertaking of another EEA undertaking and that EEA undertaking does not prepare IAS group accounts.

(7) In this section "EEA undertaking" means an undertaking established under the law of any part of the United Kingdom or the law of any other EEA State.

(8) This section is subject to the exemptions provided by sections 228 (parent companies included in accounts of larger EEA group), 228A (parent companies included in non-EEA group accounts), 229(5) (all subsidiary undertakings excluded from consolidation) and 248 (small and medium-sized groups).

227A Companies Act group accounts

(1) Companies Act group accounts must comprise -

- (a) a consolidated balance sheet dealing with the state of affairs of the parent company and its subsidiary undertakings, and
- (b) a consolidated profit and loss account dealing with the profit or loss of the parent company and its subsidiary undertakings.

(2) The accounts must give a true and fair view of the state of affairs as at the end of the financial year, and the profit or loss for the financial year, of the undertakings included in the consolidation as a whole, so far as concerns members of the company.

(3) Companies Act group accounts must comply with the provisions of Schedule 4A as to the form and content of the consolidated balance sheet and consolidated profit and loss account and additional information to be provided by way of notes to the accounts.

(4) Where compliance with the provisions of that Schedule, and the other provisions of this Act as to the matters to be included in a company's group accounts or in notes to those accounts, would not be sufficient to give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.

(5) If in special circumstances compliance with any of those provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent necessary to give a true and fair view.

(6) Particulars of any such departure, the reasons for it and its effect must be given in a note to the accounts.

227B IAS group accounts

Where the directors of a parent company prepare IAS group accounts, they must state in the notes to those accounts that the accounts have been prepared in accordance with international accounting standards.

227C Consistency of accounts

(1) The directors of a parent company that prepares group accounts must secure that the same financial reporting framework is applied in the preparation of -

- (a) the individual accounts of its subsidiary undertakings, and
- (b) the individual accounts of the parent company,

except to the extent that in their opinion there are good reasons for not doing so.

(2) Subsection (1) only applies to accounts of subsidiary undertakings which are required to be prepared under this Part.

(3) Subsection (1) does not require accounts of undertakings which are charities to be prepared using the same financial reporting framework as accounts of undertakings which are not charities.

(4) Subsection (1)(b) does not apply where-

- (a) the directors of a parent company are required to prepare IAS group accounts under Article 4 of the IAS Regulation, and
- (b) the parent company prepares IAS individual accounts."

3. Schedule 1 (consequential amendments to the 1985 Act) has effect.

PART 3

Other modifications of provisions relating to accounts

Further exemption for parent companies included in accounts of larger group

4. After section 228 of the 1985 Act insert the following -

Exemption for parent companies included in non-EEA group accounts

228A.-(1) A company is exempt from the requirement to prepare group accounts if -

(a) it is a wholly owned subsidiary of another undertaking (its “parent undertaking”), and

(b) that parent undertaking is not established under the law of an EEA State.

(2) Exemption is conditional upon compliance with all of the following conditions -

(a) that the company and all of its subsidiary undertakings are included in consolidated accounts for a larger group drawn up to the same date, or to an earlier date in the same financial year by a parent undertaking;

(b) that those accounts and, where appropriate, the group’s annual report, are drawn up in accordance with the provisions of the Seventh Directive (83/349/EEC) (where applicable as modified by the provisions of the Bank Accounts Directive (86/635/EEC) or the Insurance Accounts Directive (91/674/EEC), or in a manner equivalent to consolidated accounts and consolidated annual reports so drawn up;

(c) that the consolidated accounts are audited by one or more persons authorised to audit accounts under the law under which the parent undertaking which draws them up is established;

(d) that the company discloses in its individual accounts that it is exempt from the obligation to prepare and deliver group accounts;

(e) that the company states in its individual accounts the name of the parent undertaking which draws up the group accounts referred to above and -

(i) if it is incorporated outside Great Britain, the country in which it is incorporated, and

(ii) if it is unincorporated, the address of its principal place of business;

(f) that the company delivers to the registrar, within the period allowed for delivering its individual accounts, copies of the group accounts and, where appropriate, of the consolidated annual report, together with the auditors’ report on them;

(g) subject to section 710B(6) (delivery of certain Welsh documents without a translation) that if any document comprised in accounts and reports delivered in accordance with paragraph (f) is in a language other than English, there is annexed to the copy of that document delivered a translation of it into English, certified in the prescribed manner to be a correct translation.

(3) The exemption does not apply to a company any of whose securities are admitted to trading on a regulated market of any EEA State within the meaning of Article 1(13) of Council Directive 93/22/EEC on investment services in the securities field.

(4) Shares held by directors of a company for the purpose of complying with any share qualification requirement shall be disregarded in determining for the purposes of subsection (1)(a) whether the company is a wholly-owned subsidiary.

(5) In subsection (3) "securities" includes -

(a) shares and stock,

(b) debentures, including debenture stock, loan stock, bonds, certificates of deposit and other instruments creating or acknowledging indebtedness,

(c) warrants or other instruments entitling the holder to subscribe for securities falling within paragraph (a) or (b), and

(d) certificates or other instruments which confer -

(i) property rights in respect of a security falling within paragraph (a), (b) or (c),

(ii) any right to acquire, dispose of, underwrite or convert a security, being a right to which the holder would be entitled if he held any such security to which the certificate or other instrument relates, or

(iii) a contractual right (other than an option) to acquire any such security otherwise than by subscription."

Amendment of section 229

5. In section 229 of the 1985 Act (subsidiary undertakings included in the consolidation)¹⁹ -

(a) in subsection (3)(c), omit from "and the undertaking" to the end, and

(b) omit subsection (4).

Amendment of section 235

6.-(1) Section 235 of the 1985 Act (auditors' report)²⁰ is amended as follows.

(2) For subsection (2) substitute -

(1A) The auditors' report shall include -

¹⁹ Section 229 was substituted by section 5 of the Companies Act 1989.

²⁰ Section 235 was substituted by section 9 of the Companies Act 1989, and amended by regulation 4 of S.I. 2002/1986.

(a) an introduction identifying the annual accounts that are the subject of the audit and the financial reporting framework that has been applied in their preparation;

(b) a description of the scope of the audit identifying the auditing standards in accordance with which the audit was conducted.

(1B) The report shall state clearly whether in the auditors' opinion the annual accounts have been properly prepared in accordance with the requirements of this Act (and, where applicable, Article 4 of the IAS Regulation).

(2) The report shall state in particular whether the annual accounts give a true and fair view in accordance with the relevant financial reporting framework -

(a) in the case of an individual balance sheet, of the state of affairs of the company as at the end of the financial year,

(b) in the case of an individual profit and loss account, of the profit or loss of the company for the financial year,

(c) in the case of group accounts, of the state of affairs as at the end of the financial year and of the profit or loss for the financial year, of the undertakings included in the consolidation as a whole, so far as concerns members of the company.

(2A) The auditors' report -

(a) shall be either unqualified or qualified, and

(b) shall include a reference to any matters to which the auditors wish to draw attention by way of emphasis without qualifying the report."

Amendment of section 236

7. In section 236(1) of the 1985 Act (signature of auditors' report)²¹, after "signed" insert "and dated".

Amendment of section 240

8.-(1) In section 240(3) of the 1985 Act (requirements in connection with publication of accounts)²² -

(a) at the end of paragraph (c) omit "and", and

(b) for paragraph (d) substitute -

"(d) whether any such auditors' report -

21 Section 236 was substituted by section 9 of the Companies Act 1989.

22 Section 240 was substituted by section 10 of the Companies Act 1989, and amended by regulation 4 of, and paragraph 1 of Schedule 1 to, S.I. 1994/1935.

(i) was qualified or unqualified, or included a reference to any matters to which the auditors drew attention by way of emphasis without qualifying the report, or

(ii) contained a statement under section 237(2) or (3) (accounting records or returns inadequate, accounts not agreeing with records and returns or failure to obtain necessary information and explanations); and

(e) whether any report made for the purposes of section 249A(2) was qualified;”

Amendment of section 258

9. (1) In section 258(4) of the 1985 Act (parent and subsidiary undertakings)²³, omit “ it has a participating interest in the undertaking and”.

(2) The modification of section 258(4) in paragraph (1) also applies for the purposes of the Building Societies Act 1986²⁴.

Amendment of Schedules

10. (1) Schedule 4 to the 1985 Act (form and content of company accounts)²⁵ is amended in accordance with Schedule 2 to these Regulations.

(2) Schedule 8 to the 1985 Act (form and content of accounts prepared by small companies)²⁶ is amended in accordance with Schedule 3 to these Regulations.

(3) Schedule 8A to the 1985 Act (form and content of abbreviated accounts of small companies delivered to registrar)²⁷ is amended in accordance with Schedule 4 to these Regulations.

(4) Schedule 9 to the 1985 Act (form and content of accounts of banking companies and groups)²⁸ is amended in accordance with Schedule 5 to these Regulations.

(5) Schedule 9A to the 1985 Act (form and content of accounts of insurance companies and groups)²⁹ is amended in accordance with Schedule 6 to these Regulations.

23 Section 258 was substituted by section 21(1) of the Companies Act 1989.

24 1986 c. 53 (as amended by the Companies Act 1989 and the Building Societies Act 1997).

25 Schedule 4 was amended by section 4(2) of, and Schedule 1 to, the Companies Act 1989.

26 Schedule 8 was substituted by regulation 2(2) of, and Schedule 1 to, S.I. 1997/220.

27 Schedule 8A was inserted by regulation 2(3) of, and Schedule 2 to, S.I. 1997/220.

28 Parts I to III of Schedule 9 were inserted before a re-numbered Schedule 9A by regulation 5(1) of, and Schedule 1 to, S.I. 1991/2705. Part IV of Schedule 9 was substituted by section 18(3) and (4) of, and Part IV of Schedule 7 to, the Companies Act 1989.

29 Parts I and II of Schedule 9 to the Companies Act 1985 were formed into a new Schedule 9A by regulation 5(1) of S.I. 1991/2705. A new Schedule 9A was substituted by regulation 4 of, and Schedule 1 to, S.I. 1993/3246.

Minor and consequential amendments

11. Schedule 7 to these Regulations makes minor and consequential amendments.

2004 Minister of State for Industry and the Regions and Deputy Minister for Women and Equality,

Department of Trade and Industry.

SCHEDULE 1 Regulation 3

IAS ACCOUNTS: CONSEQUENTIAL AMENDMENTS TO 1985 ACT

1. In section 152(2) of the 1985 Act (definition of “net assets” for Chapter 6 of Part 5), after “Schedule 4” insert “that is made in Companies Act individual accounts and any provision that is made in IAS individual accounts”.
2. In section 172(2) of the 1985 Act (determination of availability of profits where private company wishes to redeem or purchase own shares out of capital), in paragraph (b) -
 - (a) at the beginning insert “the following provisions -
 - (i) where the company prepares Companies Act individual accounts,”;
 - (ii) where the company prepares IAS individual accounts, provisions of any kind”.
 - (b) after “etc)” insert “, and
 - (i) where the company prepares IAS individual accounts, provisions of any kind”.
3. In section 221 of the 1985 Act (duty to keep accounting records)³⁰, in subsections (1)(b) and (4) -
 - (a) for “any balance sheet and profit and loss account prepared under this Part complies” substitute “any accounts required to be prepared under this Part comply”; and
 - (b) at the end insert “(and, where applicable, of Article 4 of the IAS Regulation)”.
4. In section 222(3)(b) of the 1985 Act (accounts and returns to be sent to Great Britain)³¹ -
 - (a) for “the company’s balance sheet and profit and loss account” substitute “the accounts required to be prepared under this Part”; and
 - (b) at the end insert “(and, where applicable, Article 4 of the IAS Regulation)”.
5. In section 228 of the 1985 Act (exemption from obligation to prepare group accounts for parent companies included in accounts of larger group)³², in subsection (2)(b) at the end insert “or in accordance with international accounting standards”.
6. In section 229 of the 1985 Act (subsidiary undertakings included in the consolidation) -
 - (a) in subsection (1) -

³⁰ Section 221 was substituted by section 2 of the Companies Act 1989.

³¹ Section 222 was substituted by section 2 of the Companies Act 1989.

³² Section 228 was substituted by section 5(3) of the Companies Act 1989, and amended by regulation 4 of S.I. 1992/3178, by regulation 5(1) of, and paragraph 1 of Schedule 2 to, S.I. 1993/3246, by regulation 4 of S.I. 1996/189 and by section 30 of the Welsh Language Act 1993 (c.38).

(i) at the beginning insert "In the case of Companies Act group accounts,";

(ii) omit "or required";

(b) in each of subsections (2) and (3), after "consolidation" insert "in Companies Act group accounts";

(c) for subsection (5) substitute -

"(5) A parent company is exempt from the requirement to prepare group accounts if under subsection (2) or (3) all of its subsidiary undertakings could be excluded from consolidation in Companies Act group accounts."

7. In section 230 of the 1985 Act (treatment of individual profit and loss account where group accounts prepared)³³, in subsection (2) at the beginning insert "Where the company prepares Companies Act individual accounts,".

8. After section 231 of the 1985 Act insert-

"231A Disclosure required in notes to individual accounts: particulars of staff

(1) The following information with respect to the employees of the company shall be given in notes to the company's annual accounts-

(a) the average number of persons employed by the company in the financial year, and

(b) the average number of persons so employed within each category of persons employed by the company.

(2) The average number required by subsection (1)(a) or (b) shall be determined by dividing the relevant annual number by the number of months in the financial year.

(3) The relevant annual number shall be determined by ascertaining for each month in the financial year-

(a) for the purposes of subsection (1)(a), the number of persons employed under contracts of service by the company in that month (whether throughout the month or not);

(b) for the purposes of subsection (1)(b), the number of persons in the category in question of persons so employed;

and, in either case, adding together all the monthly numbers.

(4) In respect of all persons employed by the company during the financial year who are taken into account in determining the relevant

³³ Section 230 was substituted by section 5(4) of the Companies Act 1989.

annual number for the purposes of subsection (1)(a) there shall also be stated the aggregate amounts respectively of-

- (a) wages and salaries paid or payable in respect of that year to those persons;
- (b) social security costs incurred by the company on their behalf; and
- (c) other pension costs so incurred;

This does not apply in so far as those amounts, or any of them, are stated elsewhere in the company's accounts.

(5) The categories of person employed by the company by reference to which the number required to be disclosed by subsection (1)(b) is to be determined shall be such as the directors may select, having regard to the manner in which the company's activities are organised.

(6) This section applies in relation to group accounts as if the undertakings included in the consolidation were a single company.

(7) In this section "social security costs" and "pension costs" have the same meaning as in Schedule 4 (see paragraph 94(1) and (2) of that Schedule)."

9. In section 233(5) of the 1985 Act (criminal penalty for failing to comply with accounting requirements)³⁴, after "requirements of this Act" insert "(or, where applicable, of Article 4 of the IAS Regulation)".

10. (1) In sections 245 to 245C of the 1985 Act (revision of defective accounts or reports)³⁵, after "requirements of this Act", wherever occurring, insert "(or, where applicable, of Article 4 of the IAS Regulation)".

(2) That expression occurs in section 245(1) and (2), in section 245A(1), in section 245B(1), (4) and (5) and in section 245C(1).

11. (1) Section 246 of the 1985 Act (special provisions for small companies)³⁶ is amended as follows.

(2) In subsection (2) -

- (a) after "for the year" insert "are Companies Act individual accounts and"; and
- (b) for "section 226" substitute "section 226A".

(3) In subsection (5)(c), after "if" insert "they prepare Companies Act individual accounts and".

³⁴ Section 233 was substituted by section 7 of the Companies Act 1989.

³⁵ Sections 245 to 245C were inserted by section 12 of the Companies Act 1989. Section 245 was amended by regulation 4 of, and paragraph 2 in Part I of Schedule 1 to, S.I. 1994/1935, and by regulation 10 of S.I. 2002/1986. Section 245B was also amended by regulation 10 of S.I. 2002/1986.

³⁶ Section 246 was substituted by section 13 of the Companies Act 1989, and amended by regulation 2(1) of S.I. 1997/220, by regulation 6(1) of S.I. 1997/550 and by regulation 8(1) of S.I. 2000/1430.

12. In section 246A(1) of the 1985 Act (special provisions for medium-sized companies)³⁷, in subsection (1) at the end insert “and its directors prepare Companies Act individual accounts for that year”.

13. In section 247 of the 1985 Act (qualification of company as small or medium-sized)³⁸ in subsection (5) -

(a) omit “and” at the end of paragraph (a), and

(b) after paragraph (b) insert “and-

(c) where the company prepares IAS individual accounts, the aggregate of the amounts shown as assets in the balance sheet.”

14. In section 248A(1)(b) of the 1985 Act (group accounts prepared by small company)³⁹ after “preparing” insert “Companies Act”.

15. In section 249 of the 1985 Act (ascertaining aggregate figures for group qualifying as small or medium-sized)⁴⁰, in subsection (4) for “by Schedule 4A in the case of group accounts” substitute “in the case of Companies Act group accounts by Schedule 4A and in the case of IAS group accounts by international accounting standards,”.

16. In section 249C of the 1985 Act (report required for the purposes of exemption from audit under section 249A)⁴¹, in subsection (6)(a), for “section 226(3)” substitute “section 226A(3)”.

17. In section 255 of the 1985 Act (special provisions for banking and insurance companies)⁴², after subsection (4) insert -

“(4A) References to Companies Act individual accounts include accounts prepared in accordance with this section.

(4B) This section does not apply to banking companies and insurance companies which prepare IAS individual accounts.”

18. (1) Section 255A of the 1985 Act (special provisions for banking and insurance groups)⁴³ is amended as follows.

(2) In subsection (6)(a), for “section 227(5) and (6)” substitute “section 227A(4) and (5)”.

37 Section 246A was inserted by regulation 3 of S.I. 1997/220.

38 Section 247 was substituted by section 13(1) of the Companies Act 1989, and amended by regulation 5 of S.I. 1992/2452, by regulation 8 of S.I. 1996/189 and by regulation 7 of S.I. 1997/220.

39 Section 248A was inserted by regulation 6 of S.I. 1997/220.

40 Section 249 was substituted by section 13 of the Companies Act 1989, and amended by regulation 6 of S.I. 1992/2452.

41 Section 249C was inserted by regulation 2 of S.I. 1994/1935, and amended by regulation 7(3) of S.I. 1997/220 and by regulation 8(3) of S.I. 2000/1430.

42 Section 255 (as substituted by section 18 of the Companies Act 1989) was substituted by regulation 3 of S.I. 1991/2705, and amended by regulation 2 of S.I. 1993/3246.

43 Section 255A (as inserted by section 18 of the Companies Act 1989) was substituted by regulation 3 of S.I. 1991/2705, and amended by regulation 3 of S.I. 1993/3246 and by regulation 15 of S.I. 1996/189.

(3) After subsection (6) insert -

“(6A) References to Companies Act group accounts include accounts prepared in accordance with subsections (1) to (3).

(6B) Subsections (1) to (3) and (6) do not apply to parent companies of banking groups or insurance groups which prepare IAS group accounts.”

19. In section 261(2) of the 1985 Act (notes to the accounts)⁴⁴, after “any provision of this Act” insert “or international accounting standards”.

20. (1) Section 262 of the 1985 Act (minor definitions)⁴⁵ is amended as follows.

(2) In subsection (1) -

(a) at the appropriate place insert -

““Companies Act accounts” means Companies Act individual accounts or Companies Act group accounts;”;

(b) at the appropriate place insert -

““IAS accounts” means IAS individual accounts or IAS group accounts;”;

(c) at the appropriate place insert -

““IAS Regulation” means EC Regulation No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards;”⁴⁶;

(d) at the appropriate place insert -

““international accounting standards” means the international accounting standards, within the meaning of the IAS Regulation, adopted from time to time by the European Commission in accordance with that Regulation;”;

(e) at the appropriate place insert -

““profit and loss account”, in relation to a company which prepares IAS accounts, includes an income statement or other equivalent financial statement required to be prepared by international accounting standards;”;

(f) omit the definition of “true and fair view”.

⁴⁴ Section 261 was substituted by section 22 of the Companies Act 1989.

⁴⁵ Section 262 was substituted by section 22 of the Companies Act 1989, and amended by regulation 7 of S.I. 1992/3178, by regulation 12(1) of S.I. 1996/189, by regulation 4 of S.I. 1997/2306, by regulation 2 of S.I. 2000/2952, by article 16(1) of S.I. 2000/3373, by regulation 2 of S.I. 2002/765 and by regulation 10 of S.I. 2002/1986.

⁴⁶ Official Journal of 11th September 2002 (O.J.L243).

(3) After subsection (2) insert -

“(2A) References in this Part to accounts giving a “true and fair view” are references -

(a) in the case of Companies Act individual accounts, to the requirement under section 226A that such accounts give a true and fair view;

(b) in the case of Companies Act group accounts, to the requirement under section 227A that such accounts give a true and fair view; and

(c) in the case of IAS accounts, to the equivalent requirement under international accounting standards.”

21. (1) Section 262A of the 1985 Act (index of defined expressions)⁴⁷ is amended as follows.

(2) At the appropriate places insert the following defined expressions-

“Companies Act accounts	Section 262(1)”
“Companies Act group accounts 225A(6A)”	Sections 227(2) and 225A(6A)”
“Companies Act individual accounts “group accounts	Sections 226(2) and 225(4A)” Section 227(1)”
“IAS accounts	Section 262(1)”
“IAS group accounts	Section 227(2) and (3)”
“IAS individual accounts	Section 226(2)”
“IAS Regulation	Section 262(1)”
“international accounting standards	Section 262(1)”

(3) After the entry for “profit and loss account (includes notes)” insert -

“(in relation to IAS accounts) Section 262(1)”

(4) For the entry for “true and fair view” substitute -

“true and fair view Section 262(2A)”

22. In section 264(2) of the 1985 Act (restriction on distribution of assets), after “Schedule 4” insert “that is made in Companies Act accounts and any provision that is made in IAS accounts”.

23. In section 265(2) of the 1985 Act (other distributions by investment companies)⁴⁸, at the end insert “that is made in Companies Act accounts and any provision that is made in IAS accounts”.

⁴⁷ Section 262A was inserted by section 22 of the Companies Act 1989, and amended by regulation 6 of, and paragraph 3 of Schedule 2 to, S.I. 1991/2705, by regulation 5 of, and paragraph 5 of Schedule 2 to, S.I. 1993/3246, by regulation 4(2) of S.I. 1994/233, by regulation 4 of, and paragraph 3 of Schedule 1 to, S.I. 1994/1935, by regulation 12(2) of S.I. 1996/189, by regulation 7 of S.I. 1997/220, by regulation 4(4) of S.I. 1997/2306, by article 16(2) of S.I. 2000/3373 and by regulation 10 of S.I. 2002/1986

⁴⁸ Section 265 was amended by section 212 of, and paragraph 19 of Schedule 16 to, the Financial Services Act 1986, by regulation 2 of S.I. 1999/2770, by article 17 of S.I. 2001/3649 and by article 17 of S.I. 2001/3649.

24. In section 268(2)(aa) of the 1985 Act (realised profits of insurance company with long term business)⁴⁹ –

(a) after “balance sheet is” insert -

“(i) where the company prepares Companies Act individual accounts,”;

(b) at the end insert “and

(ii) where the company prepares IAS individual accounts, to that part of the balance sheet which represents accumulated profit or loss,”.

25. (1) Section 269(2) of the 1985 Act (treatment of development costs)⁵⁰ is amended as follows.

(2) Omit “and” at the end of paragraph (a).

(3) In paragraph (b) -

(a) at the beginning insert “it is stated -

(i) where the company prepares Companies Act individual accounts, in”;

(b) for “states” substitute “, or

(ii) where the company prepares IAS individual accounts, in any note to the accounts,”;

(c) for “and explains” substitute “, and

(c) the note explains”.

26. In section 270(2) of the 1985 Act (distribution to be justified by reference to company’s accounts), in paragraph (b) -

(a) at the beginning insert “the following provisions -

(i) where the company prepares Companies Act individual accounts,”;

(b) after “etc)” insert “, and

(ii) where the company prepares IAS individual accounts, provisions of any kind”.

27. In section 272(3) of the 1985 Act (interim accounts must be properly prepared)⁵¹ after “that section” insert “and sections 226A and 226B”.

28. In section 275 of the 1985 Act (treatment of assets in the relevant accounts), in subsection (1) -

49 Section 268 was amended by regulation 13 of S.I. 1996/189 and by article 18 of S.I. 2001/3649.

50 Section 269 was amended by regulation 7 of S.I. 1997/220.

51 Section 272 was amended by section 23 of, and paragraphs 5 and 6 of Schedule 10 to the Companies Act 1989, and by section 30 of the Welsh Language Act 1993 (c.38).

(a) after “264,” insert -

“(a) where the company prepares Companies Act individual accounts,”;

(b) at the end insert “and

“(b) where the company prepares IAS individual accounts, a provision of any kind is treated as a realised loss.”

29. In section 742(1) of the 1985 Act (expressions used in connection with accounts)⁵² insert at the appropriate place ““Companies Act accounts””, ““Companies Act individual accounts””, ““IAS accounts””, ““IAS individual accounts””, ““IAS Regulation”” and ““international accounting standards””.

30.–(1) Section 744A of the 1985 Act (index of defined expressions)⁵³ is amended as follows.

(2) At the appropriate places insert the following defined expressions-

“Companies Act accounts	Sections 262(1) and 742(1)“
“Companies Act individual accounts	Sections 226(2), 225(4A) and 742(1)“
“IAS accounts	Sections 262(1) and 742(1)“
“IAS individual accounts	Sections 226(2) and 742(1)“
“IAS Regulation	Sections 262(1) and 742(1)“
“international accounting standards	Sections 262(1) and 742(1)“

(3) In the definition of “profit and loss account”, in the second column, for “262(1)” substitute “262(1) and (2)”.

31. (1) Schedule 4 to the 1985 Act (form and content of company accounts)⁵⁴ is amended as follows.

(2) In Part 3 (notes to the accounts), omit paragraph 56.

(3) In Part 5 (special provisions where the company is an investment company), in paragraph 72(2) after “paragraph 89” insert “that is made in Companies Act accounts and any provision that is made in IAS accounts”.

(4) In Part 7 (interpretation) in paragraph 94(3) for “paragraph 56(1)(a)” substitute “section 231A(1)(a)”.

32. In paragraph 25 of Schedule 6 to the 1985 Act (disclosure of information: emoluments and other benefits of directors and others)⁵⁵, after “Schedule 4” insert “that is made in Companies Act accounts and any provision that is made in IAS accounts”.

⁵² Section 742 was substituted by section 23 of, and paragraph 15 of Schedule 10 to, the Companies Act 1989 and amended by article 28 of S.I. 2000/3373.

⁵³ Section 744A was inserted by section 145 of, and paragraph 20 of Schedule 19 to, the Companies Act 1989 and amended by section 79 of, and paragraph 4 of Schedule 5 to, the Criminal Justice Act 1993, regulation 4 of S.I. 1997/2306, article 30 of S.I. 2000/3373, article 31 of S.I. 2001/3649 and by regulation 4 of, and paragraph 29 of the Schedule to, S.I. 2003/1116.

⁵⁴ Schedule 4 was amended by section 4(2) of, and Schedule 1 to, the Companies Act 1989.

⁵⁵ Paragraph 25 and its internal cross-references were renumbered by section 6 of, and paragraph 4 of Schedule 4 to, the Companies Act 1989.

33. In Schedule 7 to the 1985 Act, in paragraph 12(5)(c) (identifying amounts owed to trade creditors for purposes of directors' report)⁵⁶ after "Schedule 9 or 9A" insert "or the company's accounts are IAS accounts".

34. In Part 1 of Schedule 9 to the 1985 Act (form and content of banking companies' accounts)⁵⁷ -

(a) omit paragraph 77, and

(b) in paragraph 87(c) (interpretation) for "paragraph 77(1)(a)" substitute "section 231A(1)(a)".

35. In Part 1 of Schedule 9A to the 1985 Act (form and content of insurance companies' accounts)⁵⁸ -

(a) omit paragraph 79, and

(b) in paragraph 86(c) (interpretation) for "paragraph 79(1)(a) above" substitute "section 231A(1)(a)".

36. (1) Schedule 11 to the 1985 Act (modifications of Part 8 for banking and insurance companies)⁵⁹ is amended as follows.

(2) In paragraph 5, for "section 226" substitute "sections 226, 226A and 226B".

(3) At the beginning of paragraph 9 insert "Where the company prepares Companies Act accounts, ".

(4) In paragraph 10, for "section 226" substitute "sections 226, 226A and 226B".

⁵⁶ Paragraph 12 was inserted by regulation 14 of S.I. 1996/189 and substituted by regulation 2 of S.I. 1997/571.

⁵⁷ Parts I to III of Schedule 9 were inserted before a re-numbered Schedule 9A by regulation 5 of, and Schedule 1 to, S.I. 1991/2705. Part IV of Schedule 9 was substituted by section 18(3) and (4) of and Part IV of Schedule 7 to, the Companies Act 1989.

⁵⁸ Parts I and II of Schedule 9 to the Companies Act 1985 were formed into a new Schedule 9A by regulation 5(1) of S.I. 1991/2705. A new Schedule 9A was substituted by regulation 4 of, and Schedule 1 to, S.I. 1993/3246.

⁵⁹ Schedule 11 was amended by section 23 of, and paragraph 21 of Schedule 10 to, the Companies Act 1989, by regulation 7 of, and Schedule 3 to, S.I. 1991/2705, and by regulation 5 of, and paragraph 8 of Schedule 2 to, S.I. 1993/3246 and by regulation 14 of, and Schedule 6 to, S.I. 1996/189.

SCHEDULE 2 Regulation 10(1)

FORM AND CONTENT OF COMPANY ACCOUNTS

1. Schedule 4 to the 1985 Act (form and content of company accounts) is amended as follows.
2. (1) Paragraph 3 (dividends in profit and loss account to be shown as separate items)⁶⁰ is amended as follows.
 - (2) In sub-paragraph (7)-
 - (a) in paragraph (b), for “paid and proposed” substitute “paid (other than dividends for which a liability existed at the immediately preceding balance sheet date) or which the company is liable to pay”; and
 - (b) omit paragraph (c).
 - (3) After that sub-paragraph insert -

“(7A) There shall be shown in the notes to the accounts the aggregate amount of any dividends proposed before the date of approval of the accounts which have not been shown in the profit and loss account in accordance with sub-paragraph (7)(b).”
3. After paragraph 5 insert -

“5A. The directors of a company shall, in determining how amounts are presented within items in the profit and loss account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.”
4. (1) In the Balance Sheet Formats, for “provisions for liabilities and charges”, wherever occurring, substitute “provisions for liabilities”.
 - (2) That expression occurs -
 - (a) in Balance Sheet Format 1, in Item I;
 - (b) in Balance Sheet Format 2, under the heading “LIABILITIES”, in Item B.
5. In paragraph 12(b) (extent to which liabilities and losses to be taken into account) omit “and losses” and “or are likely to arise”.
6. After paragraph 34C insert -

“Other assets which may be included at fair value

34CA. (1) This paragraph applies to -
 - (a) investment property, and
 - (b) living animals and plants,

⁶⁰ Paragraph 3(7) was amended by regulation 14(1) of, and paragraphs 1 and 2 of Schedule 1 to, S.I. 1996/189.

that, under international accounting standards, may be included in accounts at fair value.

(2) Such investment property and such living animals and plants may be included at fair value, provided that all such investment property or, as the case may be, all such living animals and plants are so included where their fair value can reliably be determined.

(3) In this paragraph, "fair value" means fair value determined in accordance with relevant international accounting standards."

7. Paragraph 34D is amended as follows -

(a) in paragraph (1), at the end insert "or an asset is valued in accordance with paragraph 34CA";

(b) in paragraph (2), after "financial instrument" insert "or of the investment property or living animal or plant".

8. After paragraph 45C insert -

"Information where investment property and living animals and plants included at fair value

45D.-(1) This paragraph applies where the amounts to be included in a company's accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 34CA.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts -

(a) the comparable amounts determined according to the historical cost accounting rules; or

(b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to -

(a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and

(b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or

required in determining those amounts according to those rules.”

9. In paragraph 46(1) (transfers to and from reserves and provisions) -

(a) in paragraph (b), for “provisions for liabilities and charges” substitute “provisions for liabilities”;

(b) in paragraph (c), for “provision for liabilities and charges” substitute “provision for liabilities”.

10. In paragraph 72(2) (distributions by investment companies), for “provision for liabilities or charges” substitute “provision for liabilities”.

11. After paragraph 82 insert -

“Investment property

82A. “Investment property” means land held to earn rent or for capital appreciation.”

12. In paragraph 89 (interpretation of references to provisions for liabilities or charges)-

(a) for “provisions for liabilities or charges” substitute “provisions for liabilities”, and

(b) for “or loss” substitute “the nature of which is clearly defined and “.

SCHEDULE 3 Regulation 10(2)

FORM AND CONTENT OF ACCOUNTS PREPARED BY SMALL COMPANIES

1. Schedule 8 to the 1985 Act (form and content of small company accounts)⁶¹ is amended as follows.
2. (1) Paragraph 3 (dividends in profit and loss account to be shown as separate items) is amended as follows.
 - (2) In sub-paragraph (7), in paragraph (b), for “paid and proposed” substitute “paid (other than dividends for which a liability existed at the immediately preceding balance sheet date) or which the company is liable to pay”.
 - (3) After that sub-paragraph insert -

“(7A) There shall be shown in the notes to the accounts the aggregate amount of any dividends proposed before the date of approval of the accounts which have not been shown in the profit and loss account in accordance with sub-paragraph (7)(b).”
3. After paragraph 5 insert -

“5A. The directors of a company shall, in determining how amounts are presented within items in the profit and loss account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.”
4. (1) In the Balance Sheet Formats, for “provisions for liabilities and charges”, wherever occurring, substitute “provisions for liabilities”.
 - (2) That expression occurs -
 - (a) in Balance Sheet Format 1, in Item I;
 - (b) in Balance Sheet Format 2, under the heading “LIABILITIES”, in Item B.
5. In paragraph 12(b) (extent to which liabilities and losses to be taken into account) omit “and losses” and “or are likely to arise”.
6. After paragraph 34C insert -

Other assets which may be included at fair value

34CA. (1) This paragraph applies to -
 - (a) investment property, and
 - (b) living animals and plants,that, under international accounting standards, may be included in accounts at fair value.

⁶¹ Schedule 8 was substituted by regulation 2(2) of, and Schedule 1 to, S.I. 1997/220.

(2) Such investment property and such living animals and plants may be included at fair value, provided that all such investment property or, as the case may be, all such living animals and plants are so included where their fair value can reliably be determined.

(3) In this paragraph, "fair value" means fair value determined in accordance with relevant international accounting standards."

7. Paragraph 34D is amended as follows -

(a) in paragraph (1), at the end insert "or an asset is valued in accordance with paragraph 34CA";

(b) in paragraph (2), after "financial instrument" insert "or of the investment property or living animal or plant".

8. After paragraph 42B insert -

Information where investment property and living animals and plants included at fair value

42C.-(1) This paragraph applies where the amounts to be included in a company's accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 34CA.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts -

(a) the comparable amounts determined according to the historical cost accounting rules; or

(b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to -

(a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and

(b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or required in determining those amounts according to those rules."

9. In paragraph 43(1)(transfers to and from reserves and provisions) -

(a) in paragraph (b), for “provisions for liabilities and charges” substitute “provisions for liabilities”;

(b) in paragraph (c), for “provision for liabilities and charges” substitute “provision for liabilities”.

10. After paragraph 53 insert -

“Investment property

53A. “Investment property” means land held to earn rent or for capital appreciation.”

11. In paragraph 58 (interpretation of references to provisions for liabilities or charges)-

(a) for “provisions for liabilities or charges” substitute “provisions for liabilities”, and

(b) for “or loss” substitute “the nature of which is clearly defined and “.

SCHEDULE 4 Regulation 10(3)

FORM AND CONTENT OF ABBREVIATED ACCOUNTS OF SMALL COMPANIES DELIVERED TO REGISTRAR

1. Schedule 8A to the 1985 Act (form and content of small company accounts delivered to registrar)⁶² is amended as follows.

2. (1) In the Balance Sheet Formats, for “provisions for liabilities and charges”, wherever occurring, substitute “provisions for liabilities”.

(2) That expression occurs -

(a) in Balance Sheet Format 1, in Item I; and

(b) in Balance Sheet Format 2, under the heading “LIABILITIES”, in Item B.

⁶² Schedule 8A was inserted by regulation 2(3) of, and Schedule 2 to, S.I. 1997/220.

SCHEDULE 5 Regulation 10(4)

FORM AND CONTENT OF ACCOUNTS OF BANKING COMPANIES AND GROUPS

1. Part 1 of Schedule 9 to the 1985 Act (form and content of accounts of banking companies and groups) is amended as follows.
2. (1) In paragraph 8 (dividends in profit and loss account to be shown as separate items)⁶³ -
 - (a) in paragraph (b) , for “paid and proposed” substitute “paid (other than dividends for which a liability existed at the immediately preceding balance sheet date) or which the company is liable to pay”, and
 - (b) omit paragraph (c).
3. After paragraph 8 insert -

“8A There shall be shown in the notes to the accounts the aggregate amount of any dividends proposed before the date of approval of the accounts which have not been shown in the profit and loss account in accordance with paragraph (8)(b).

8B. The directors of a company shall, in determining how amounts are presented within items in the profit and loss account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.”
4. In the Balance Sheet Format, under the heading “LIABILITIES” ,for “Provisions for liabilities and charges” substitute “Provisions for liabilities”.
5. In paragraph 19(b) (extent to which liabilities and losses to be taken into account) omit “and losses” and “or are likely to arise”.
6. After paragraph 46C insert -

Other assets which may be included at fair value

46CA. (1) This paragraph applies to -

 - (a) investment property, and
 - (b) living animals and plants,

that, under international accounting standards, may be included in accounts at fair value.

(2) Such investment property and such living animals and plants may be included at fair value, provided that all such investment property or, as the case may be, all such living animals and plants are so included where their fair value can reliably be determined.

63 Paragraph 8 was amended by regulation 14(6) of, and paragraphs 1 and 2 of Schedule 4 to, S.I. 1996/189.

(3) In this paragraph, "fair value" means fair value determined in accordance with relevant international accounting standards."

7. Paragraph 46D is amended as follows -

(a) in paragraph (1), at the end insert "or an asset is valued in accordance with paragraph 46CA";

(b) in paragraph (2), after "financial instrument" insert "or of the investment property or living animal or plant".

8. After paragraph 58C insert -

Information where investment property and living animals and plants included at fair value

58D.-(1) This paragraph applies where the amounts to be included in a company's accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 46CA.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts -

(a) the comparable amounts determined according to the historical cost accounting rules; or

(b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to -

(a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and

(b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or required in determining those amounts according to those rules."

9. In paragraph 59(1) (transfers to and from reserves and provisions) -

(a) in paragraph (b), for "provisions for liabilities and charges" substitute "provisions for liabilities", and

(b) in paragraph (c), for "provision for liabilities and charges"

substitute "provision for liabilities".

10. In paragraph 82 (general interpretation), at the appropriate place, insert -
"Investment property" means land held to earn rent or for capital appreciation."

11. In paragraph 85(c) (interpretation of references to provisions for liabilities or charges)-

(a) for "provisions for liabilities or charges" substitute "provisions for liabilities", and

(b) for "or loss" substitute "the nature of which is clearly defined and ".

SCHEDULE 6 Regulation 10(5)

FORM AND CONTENT OF ACCOUNTS OF INSURANCE COMPANIES AND GROUPS

1. Part 1 of Schedule 9A to the 1985 Act (form and content of accounts of insurance companies and groups) is amended as follows.
2. (1) In paragraph 5 (dividends in profit and loss account to be shown as separate items)⁶⁴ -
 - (a) in paragraph (b), for “paid and proposed” substitute “paid (other than dividends for which a liability existed at the immediately preceding balance sheet date) or which the company is liable to pay”, and
 - (b) omit paragraph (c).
3. After paragraph 5 insert -

“5A. There shall be shown in the notes to the accounts the aggregate amount of any dividends proposed before the date of approval of the accounts which have not been shown in the profit and loss account in accordance with paragraph (5)(b).”
4. After paragraph 6 insert -

“6A. The directors of a company shall, in determining how amounts are presented within items in the profit and loss account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.”
5. In the Balance Sheet Format, under the heading “LIABILITIES”, for “Provisions for other risks and charges” substitute “Provisions for other risks”.
6. In paragraph 16(b) (extent to which liabilities and losses to be taken into account) omit “and losses” and “or are likely to arise”.
7. After paragraph 29C insert -

“Other assets which may be included at fair value”

29CA. (1) This paragraph applies to -

 - (a) investment property, and
 - (b) living animals and plants,

that, under international accounting standards, may be included in accounts at fair value.

⁶⁴ Paragraph 5 was amended by regulation 14(7) of, and paragraphs 1 and 2 of Schedule 5 to, S.I. 1996/189.

(2) Such investment property and such living animals and plants may be included at fair value, provided that all such investment property or, as the case may be, all such living animals and plants are so included where their fair value can reliably be determined.

(3) In this paragraph, "fair value" means fair value determined in accordance with relevant international accounting standards."

7. Paragraph 29D is amended as follows -

(a) in paragraph (1), at the end insert "or an asset is valued in accordance with paragraph 29CA";

(b) in paragraph (2), after "financial instrument" insert "or of the investment property or living animal or plant".

8. After paragraph 65C insert -

Information where investment property and living animals and plants included at fair value

65D.-(1) This paragraph applies where the amounts to be included in a company's accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 29CA.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts -

(a) the comparable amounts determined according to the historical cost accounting rules; or

(b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to -

(a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and

(b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or required in determining those amounts according to those rules."

9. In paragraph 66(1)(b) and (c) (transfers to or from provisions)⁶⁵, for “provisions for other risks and charges” substitute “provisions for other risks”.

10. In paragraph 81 (general interpretation), at the appropriate place, insert -
““investment property” means land held to earn rent or for capital appreciation.”

11. In paragraph 84(c) (interpretation of references to provisions for risks and charges)⁶⁶ -

(a) for “provisions for other risks and charges” substitute “provisions for other risks”, and

(b) for “or loss” substitute “the nature of which is clearly defined and”.

⁶⁵ Paragraph 66 was amended by regulation 14 of, and paragraphs 1 and 10 of Schedule 5 to, S.I. 1996/189.

⁶⁶ Paragraph 84(c) was amended by regulation 14(7) of, and paragraphs 1 and 18 of Schedule 5 to, S.I. 1996/189.

SCHEDULE 7 Regulation 11

MINOR AND CONSEQUENTIAL AMENDMENTS

1. In section 152(2) of the 1985 Act (definition of “net assets” for Chapter 6 of Part 5), for “provision for liabilities or charges” substitute “provision for liabilities”.
2. In section 154(2)(b) of the 1985 Act (definition of “liabilities” for the purposes of the “net asset” test) for “or loss” substitute “the nature of which is clearly defined and”.
3. (1) Section 228 of the 1985 Act (exemption for parent companies included in accounts of larger group) is amended as follows.

(2) In subsections (1) and (3)(a) for “a member State of the European Economic Community” substitute “an EEA State”.

(3) In subsection (3), omit from “listed” to the end, and substitute “admitted to trading on a regulated market of any EEA State within the meaning of Article 1(13) of Council Directive 93/22/EEC on investment services in the securities field”.
4. In section 231(5)(b) of the 1985 Act (disclosure required in notes to accounts of undertakings excluded from consolidation)⁶⁷, omit “or (4)”.
5. Section 243 of the 1985 Act (accounts of subsidiary undertakings to be appended in certain cases)⁶⁸ is repealed.
6. In section 260 of the 1985 Act (definition of “participating interest”)⁶⁹, omit subsection (5).
7. In section 264(2) of the 1985 Act (restriction on distribution of assets), for “provision for liabilities or charges” substitute “provision for liabilities”.
8. In section 265(2) of the 1985 Act (other distributions by investment companies), for “provision for liabilities or charges” substitute “provision for liabilities”.
9. Paragraph 18 of Schedule 4A to the 1985 Act (interests in subsidiary undertakings excluded from consolidation)⁷⁰ is repealed.
10. In paragraph 25 of Schedule 6 to the 1985 Act (disclosure of information: emoluments and other benefits of directors and others), for “provisions for liabilities or charges” substitute “provisions for liabilities”.
11. Paragraph 1 in Part 2 of Schedule 9 to the 1985 Act (undertakings to be included in consolidation) is repealed.

⁶⁷ Section 231 was substituted by section 6(1) of the Companies Act 1989, and subsection (5) was amended by regulation 15 of S.I. 1996/189.

⁶⁸ Section 243 was substituted by section 11 of the Companies Act 1989, and amended by regulation 2 of S.I. 1992/1083, and sections 30 and 35 of, and Schedule 2 to, the Welsh Language Act 1993.

⁶⁹ Section 260 was substituted by section 22 of the Companies Act 1989, and amended by regulation 5(1) of, and paragraph 4 of Schedule 2 to, S.I. 1993/3246, and by regulation 7(5) of S.I. 1997/220.

⁷⁰ Schedule 4A was inserted by section 5(2) of, and Schedule 2 to, the Companies Act 1989.

Draft Statutory Instruments for building societies

Draft Order laid before Parliament under section 104 of the Building Societies Act 1986, for approval by resolution of each House of Parliament.

DRAFT STATUTORY INSTRUMENTS

2004 No.

BUILDING SOCIETIES

The Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004

Made.....2004

Coming into force2004

The Treasury, in exercise of the powers conferred upon them by section 104 of the Building Societies Act 1986⁽¹⁾ hereby make the following Order, of which a draft has been laid before Parliament in accordance with section 104(5) of that Act and approved by both Houses of Parliament:

PART 1

General

Citation, commencement and interpretation

1. – This Order may be cited as the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004.

(2) This Order comes into force on the day after the day on which it is made and has effect as respects building societies' financial years which begin on or after 1st January 2005 (the "commencement date").

(3) In this Order "the 1986 Act" means the Building Societies Act 1986.

¹ 1986 c. 53 (as amended by the Companies Act 1989 and the Building Societies Act 1997).

PART 2

Accounts prepared in accordance with international accounting standards

Preparation of individual and group accounts in accordance with the IAS Regulation

2. For sections 72 and 73 of the 1986 Act substitute -

“72A. Duty to prepare individual accounts

(1) The directors of every building society must prepare accounts for the society for each of its financial years.

Those accounts are referred to in this Part as the society’s “individual accounts”.

(2) A society’s individual accounts may be prepared -

(a) in accordance with section 72B (“Building Societies Act individual accounts”), or

(b) in accordance with international accounting standards (“IAS individual accounts”).

This subsection is subject to subsection (3) and section 72I (consistency of accounts).

(3) Where the directors of a society have prepared IAS individual accounts for a financial year, they must prepare all subsequent individual accounts for the society in accordance with international accounting standards.

72B. Building Societies Act individual accounts

(1) Building Societies Act individual accounts must comprise -

(a) a balance sheet as at the last day of the financial year, and

(b) an income and expenditure account.

(2) The balance sheet must give a true and fair view of the state of affairs of the society as at the end of the financial year; and the income and expenditure account must give a true and fair view of the income and expenditure of the society for the financial year.

(3) Building Societies Act individual accounts must comply with the requirements of regulations made under section 72C as to the form and content of the balance sheet and income and expenditure account and additional information to be provided by way of notes to the accounts or otherwise.

(4) Where compliance with the provisions of those regulations, and the other provisions of this Act as to the matters to be included in a society’s individual accounts or in notes to those accounts, would not be sufficient to

give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.

(5) If in special circumstances compliance with any of those provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent necessary to give a true and fair view.

(6) Particulars of any such departure, the reasons for it and its effect must be given in a note to the accounts.

(7) The Treasury may by regulations -

- (a) add to the classes of documents to be comprised in a society's Building Societies Act individual accounts under subsection (1);
- (b) make provision as to the matters to be included in any document so added;
- (c) modify the requirements of this Part as to the matters to be stated in any document comprised in the society's Building Societies Act individual accounts; and
- (d) reduce the classes of documents to be comprised in a society's Building Societies Act individual accounts.

(8) Regulations under subsection (7) -

- (a) may make different provision for different descriptions of society, and
- (b) may include incidental and supplementary provisions.

(9) The power to make regulations under subsection (7) is exercisable by statutory instrument which shall be subject to annulment in pursuance of a resolution of either House of Parliament.

72C. Contents and form of Building Societies Act individual accounts

(1) The Treasury shall by regulations make provision with respect to the contents and the form of Building Societies Act individual accounts.

(2) The Treasury may by regulations make provision with respect to additional information to be contained in Building Societies Act individual accounts, whether in the form of notes or otherwise.

(3) Without prejudice to the generality of subsections (1) and (2), the regulations may -

- (a) prescribe accounting principles and rules;
- (b) require corresponding information for a preceding financial year;
- (c) require the accounts of societies to deal also with their associated undertakings;

- (d) make different provision for different descriptions of society;
- (e) require the accounts to give particulars of the emoluments, pensions, compensation for loss of office and financial interests of directors, other officers and employees of prescribed descriptions of the society.

(4) It is the duty of every director, other officer and employee of a building society as respects whom particulars are required to be given in the accounts, by virtue of subsection (3)(e) above, to give notice of such matters to the society as may be necessary to enable the society to give those particulars in the accounts.

(5) The power to make regulations under this section is exercisable by statutory instrument which shall be subject to annulment in pursuance of a resolution of either House of Parliament.

72D. IAS individual accounts

Where the directors of a building society prepare IAS individual accounts, they must state in the notes to those accounts that the accounts have been prepared in accordance with international accounting standards.

72E. Duty to prepare group accounts

(1) If at the end of a financial year a building society has subsidiary undertakings, the directors, as well as preparing individual accounts for the year, must prepare accounts for the year for the society and those undertakings taken as a whole.

Those accounts are referred to in this Part as the society's "group accounts".

(2) Certain societies are obliged by Article 4 of the IAS Regulation to prepare their group accounts in accordance with international accounting standards ("IAS group accounts").

(3) The group accounts of other societies may be prepared -

(a) in accordance with section 72F ("Building Societies Act group accounts"), or

(b) in accordance with international accounting standards ("IAS group accounts").

This subsection is subject to subsection (4) and section 72I (consistency of accounts).

(4) Where the directors of a parent company have prepared IAS group accounts for a financial year, they must prepare all subsequent group accounts for the company in accordance with international accounting standards.

(5) The directors of a society which has subsidiary undertakings must secure that, except where in their opinion there are good reasons against it, the financial year of each of its subsidiary undertakings coincides with the society's own financial year.

72F. Building Societies Act group accounts

(1) Building Societies Act group accounts must comprise -

- (a) a balance sheet dealing with the state of affairs of the building society and its subsidiary undertakings, and
- (b) an income and expenditure account showing the income and expenditure for the society and its subsidiary undertakings.

(2) The accounts must give a true and fair view of the state of affairs as at the end of the financial year, and the income and expenditure for the financial year of the society and the subsidiary undertakings included in the group accounts as a whole, so far as concerns members of the company.

(3) Building Societies Act group accounts must comply with the requirements of regulations made under section 72G as to the form and content of the group accounts and additional information to be provided by way of notes to the accounts or otherwise.

(4) Where compliance with the provisions of those regulations as to the matters to be included in a society's group accounts or in notes to those accounts, would not be sufficient to give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.

(5) If in special circumstances compliance with any of those provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent necessary to give a true and fair view.

(6) Particulars of any such departure, the reasons for it and its effect must be given in a note to the accounts.

(7) The Treasury may by regulations -

- (a) add to the classes of documents to be comprised in a society's Building Societies Act group accounts under subsection (1);
- (b) make provision as to the matters to be included in any document so added;
- (c) modify the requirements of this Part as to the matters to be stated in any document comprised in the society's Building Societies Act group accounts; and
- (d) reduce the classes of documents to be comprised in a society's Building Societies Act group accounts.

(8) Regulations under subsection (7) -

- (a) may make different provision for different descriptions of society, and
- (b) may include incidental and supplementary provisions.

(9) The power to make regulations under subsection (7) is exercisable by statutory instrument which shall be subject to annulment in pursuance of a resolution of either House of Parliament.

72G. Contents and form of Building Societies Act group accounts

(1) The Treasury shall by regulations make provision with respect to the contents and the form of Building Societies Act group accounts.

(2) The Treasury may by regulations make provision with respect to additional information to be contained in Building Societies Act group accounts, whether in the form of notes or otherwise.

(3) Without prejudice to the generality of subsections (1) and (2), the regulations may -

- (a) prescribe accounting principles and rules;
- (b) require corresponding information for a preceding financial year;
- (c) require the accounts of societies to deal also with their associated undertakings;
- (d) make different provision for different descriptions of society;
- (e) require the accounts to give particulars of the emoluments, pensions, compensation for loss of office and financial interests of directors, other officers and employees of prescribed descriptions of the society;

and may permit group accounts to be prepared in other than consolidated form.

(4) It is the duty of every director, other officer and employee of a building society as respects whom particulars are required to be given in the accounts, by virtue of subsection (3)(e) above, to give notice of such matters to the society as may be necessary to enable the society to give those particulars in the accounts.

(5) The power to make regulations under this section is exercisable by statutory instrument which shall be subject to annulment in pursuance of a resolution of either House of Parliament.

72H. IAS group accounts

Where the directors of a building society prepare IAS group accounts, they must state in the notes to those accounts that the accounts have been prepared in accordance with international accounting standards.

72I. Consistency of accounts

(1) The directors of a building society that prepares group accounts must secure that the same financial reporting framework is applied in the preparation of -

- (a) the individual accounts of its subsidiary undertakings, and
- (b) the individual accounts of the building society,

except to the extent that in their opinion there are good reasons for not doing so.

(2) Subsection (1) only applies to accounts of subsidiary undertakings which are required to be prepared under Part 7 of the Companies Act 1985⁽²⁾.

(3) Subsection (1) does not require accounts of undertakings which are charities to be prepared using the same financial reporting framework as accounts of undertakings which are not charities.

(4) Subsection (1)(c) does not apply where -

- (a) the directors of a building society are required to prepare IAS group accounts under Article 4 of the IAS Regulation, and
- (b) the building society prepares IAS individual accounts."

PART 3

Other modifications of provisions relating to accounts

Duty to prepare director's report

3. - Section 75 of the 1986 Act (directors' report) is amended as follows.

(2) In subsection (1) for paragraph (a) substitute -

"(a) a fair review of the business of the society and any subsidiary undertakings it has, complying with section 75A,

(aa) a description of the principal risks and uncertainties facing the society and any subsidiary undertakings it has, and"

(3) After subsection (1A) insert -

"(1B) If the building society has subsidiary undertakings, the report may, where appropriate, give greater emphasis to those matters which are significant to the society and its subsidiary undertakings taken as a whole."

(4) Subsection (2) is omitted.

2 1985 c.6, as amended by the Companies Act 1989 (1989 c.40), S.I. 1991/2705, S.I. 1993/3246, S.I. 1994/1935, S.I. 1997/220 and S.I. 2002/1986.

Business Review

4. After section 75 of the 1986 Act insert -

“75A Business review

(1) The review required for the purposes of section 75(1) is a balanced and comprehensive analysis of -

(a) the development and performance of the business of the building society and any subsidiary undertakings it has, during the financial year, and

(b) the position of the building society and any subsidiary undertakings it has, at the end of that year,

consistent with the size and complexity of the business.

(2) The review shall, to the extent necessary for an understanding of the development, performance or position of the business of the society and any subsidiary undertakings it has, include -

(a) analysis using financial key performance indicators, and

(b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.

(3) The review shall, where appropriate, include references to and additional explanations of amounts included in the annual accounts of the society.

(4) In this section “key performance indicators” means factors by reference to which the development, performance or position of the business of the society and any subsidiary undertakings it has can be measured most effectively.”

Amendment of section 78

5. - Section 78 of the 1986 Act (auditors’ report) is amended as follows.

(2) For subsections (4) and (5) substitute -

“(3A) The auditors’ report shall include -

(a) an introduction identifying the annual accounts that are the subject of the audit and the financial reporting framework that has been applied in their preparation;

(b) a description of the scope of the audit identifying the auditing standards in accordance with which the audit was conducted.

(3B) The report shall state clearly whether in the auditors’ opinion the annual accounts have been properly prepared in accordance with the

requirements of this Act (and, where applicable, Article 4 of the IAS Regulation).

(4) The report shall state in particular whether the annual accounts give a true and fair view in accordance with the relevant financial reporting framework -

(a) in the case of an individual balance sheet, of the state of affairs of the society as at the end of the financial year,

(b) in the case of an individual income and expenditure account, of the income and expenditure of the society for the financial year,

(c) in the case of group accounts, of the state of affairs as at the end of the financial year and the income and expenditure for the financial year of the society and the subsidiary undertakings dealt with in the group accounts, so far as concerns members of the society.

(4A) The auditors' report -

(a) shall be either unqualified or qualified, and

(b) shall include a reference to any matters to which the statutory auditors wish to draw attention by way of emphasis without qualifying the report."

Insertion of new section 78A

6. After section 78 of the 1986 Act insert the following -

"78A. Signature of auditors' report

(1) The auditors' report shall state the names of the auditors and be signed and dated by them.

(2) Every copy of the auditors report which is laid before the building society at the annual general meeting or which is otherwise circulated, published or issued, shall state the names of the auditors.

(3) If a copy of the auditors' report is laid before the society or otherwise circulated, published or issued without the required statement of the auditors' names, the society and every officer of it who is in default is guilty of an offence and liable on summary conviction to a fine not exceeding level 3 on the standard scale.

(4) References in this section to signature by the auditors are, where the office of auditor is held by a body corporate or partnership, to signature in the name of the body corporate or partnership by a person authorised to sign on its behalf."

Insertion of new section 81A

7. After section 81 of the 1986 Act insert the following -

“81A. Requirements in connection with publication of accounts

(1) If a building society publishes any of its statutory accounts, they must be accompanied by the relevant auditors’ report under section 78.

(2) A building society which is required to prepare group accounts for a financial year shall not publish its statutory individual accounts for that year without also publishing with them its statutory group accounts.

(3) If a building society publishes non-statutory accounts, it shall publish with them a statement indicating -

- (a) that they are not the society’s statutory accounts,
- (b) whether statutory accounts dealing with any financial year with which the non-statutory accounts purport to deal have been prepared,
- (c) whether the society’s auditors have made a report under section 78 on the statutory accounts for any financial year, or
- (d) whether any such auditors’ report -
 - (i) was qualified or unqualified, or included a reference to any matters to which the auditors drew attention by way of emphasis without qualifying the report, or
 - (ii) contained a statement under section 79(6) (failure to obtain necessary information and explanations);

and it shall not publish with any non-statutory accounts any auditors’ report under section 78.

(4) For the purposes of this section a building society shall be regarded as publishing a document if it publishes issues or circulates it or otherwise makes it available for public inspection in a manner calculated to invite members of the public generally, or any class of members of the public, to read it.

(5) References in this section to a building society’s statutory accounts are to its annual accounts as required to be laid before the society under section 81; and references to the publication by a society of “non-statutory accounts” are to the publication of -

- (a) any balance sheet or income and expenditure account relating to, or purporting to deal with, a financial year of the society, or
- (b) an account in any form purporting to be a balance sheet or income and expenditure account for the group consisting of the society and its subsidiary undertakings relating to, or purporting to deal with, a

financial year of the company,
otherwise than as part of the company's statutory accounts or summary financial statement prepared under section 76.

(6) A building society which contravenes any provision of this section, and any officer of it who is in default, is guilty of an offence and liable to a fine not exceeding level 3 on the standard scale."

Consequential amendments

8. The Schedule to this Order (consequential amendments to the 1986 Act) has effect.

PART 4

Transitional provisions

Regulations made under sections 72 and 73

9. - Regulations made under section 72 of the 1986 Act (documents comprised in annual accounts) and in force immediately before the commencement date shall have effect as if made under sections 72B and 72F of that Act (inserted by this Order).

(2) Regulations made under section 73 of the 1986 Act (contents and form of annual accounts) and in force immediately before the commencement date shall have effect as if made under sections 72C and 72G of that Act (inserted by this Order).

2004

Two of the Lords Commissioners of Her Majesty's Treasury

EXPLANATORY NOTE

(This note is not part of the Order)

This Order makes provision to give effect to Regulation (EC) 1606/2002 of the European Parliament and of the Council on the application of international accounting standards (OJ L 243, 11/09/2002 p.1 - 4). It also implements in part Directive 2003/51/EC of the European Parliament and of the Council amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC as regards modernising the annual and consolidated accounts of certain types of companies, banks and other financial institutions to bring the preparation of those accounts more into line with international accounting standards (OJ L 178, 17/07/2003, p.16 - 22). A Transposition Note showing how the main provisions of this Directive (as it applies to building societies) will be transposed into UK law is available from HM Treasury (details to be inserted).

SCHEDULE

Consequential amendments to the 1986 Act

Article 8

1. (1) Section 6 (the lending limit) of the 1986 Act is amended as follows.
(2) In subsection (2)-
 - (a) after "the liquid" insert "or current";
 - (b) for "under section 73(7)" substitute "under section 72C or 72G, or in accordance with international accounting standards, as appropriate";
 - (c) after "the fixed" insert "or non-current".(3) In subsection (14) -
 - (a) in paragraph (a), omit "under subsection (1) of section 72"; and
 - (b) in paragraph (b), omit "under subsection (2) of that section".
2. In section 61(3A) (supplementary provisions regarding election of directors) -
 - (a) in paragraph (a), for "under section 73(7) substitute "under section 72C or 72G, or in accordance with international accounting standards, as appropriate"; and
 - (b) for "section 72" substitute "section 72A or 72E".
3. In section 71(2) of the 1986 Act (accounting records), in each of paragraphs (c) and (d), after "under this Act" insert "(and, where applicable Article 4 of the IAS Regulation)".
4. After section 72I of the 1986 Act (inserted by this order) insert -
"72J Disclosure required in notes to accounts: particulars of staff"
 - (1) The following information with respect to the employees of a building society shall be given in notes to the society's annual accounts -
 - (a) the average number of persons employed by the society in the financial year, and
 - (b) the average number of persons so employed within each category of persons employed by the society.
 - (2) The average number required by subsection (1)(a) or (b) shall be determined by dividing the relevant annual number by the number of complete calendar months in the financial year.
 - (3) The relevant annual number shall be determined by ascertaining for each complete calendar month in the financial year -

(a) for the purposes of subsection (1)(a), the number of persons employed under contracts of service by the society in that month (whether throughout the month or not);

(b) for the purposes of subsection (1)(b), the number of persons in the category in question of persons so employed;

and, in either case, adding together all the monthly numbers.

(4) In respect of all persons employed by the society during the financial year who are taken into account in determining the relevant annual number for the purposes of subsection (1)(a) there shall also be stated the aggregate amounts respectively of -

(a) wages and salaries paid or payable in respect of that year to those persons;

(b) social security costs incurred by the company on their behalf; and

(c) other pension costs so incurred.

This does not apply in so far as those amounts, or any of them, are stated elsewhere in the society's accounts.

(5) The categories of person employed by the society by reference to which the number required to be disclosed by subsection (1)(b) is to be determined shall be such as the directors may select, having regard to the manner in which the society's activities are organised.

(6) This section applies in relation to group accounts as if the undertakings included in those accounts were a single society.

(7) In this section -

(a) "social security costs" means any contribution by the society to any state social security or pension scheme, fund or arrangement;

(b) "pension costs" includes any costs incurred by the society in respect of any pension scheme established for the purpose of providing pensions for persons currently or formerly employed by the society, any sums set aside for future payment of pensions directly by the society to current or former employees and any pensions paid directly to such persons without having been first set aside."

5. After section 85 of the 1986 Act insert -

"85A Interpretation of Part 8

(1) In this Part -

"annual accounts", in relation to a building society, means -

(a) the individual accounts required by section 72A, and

(b) any group accounts required by section 72E,

together with the notes to those accounts;

“IAS accounts” means IAS individual accounts or IAS group accounts;

“IAS Regulation” means EC Regulation No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards⁽³⁾;

“income and expenditure account”, in relation to a society which prepares IAS accounts, includes an income statement or other equivalent financial statement required to be prepared by international accounting standards;

“international accounting standards” means the international accounting standards, within the meaning of the IAS Regulation, adopted from time to time by the European Commission in accordance with the IAS Regulation.

(2) References in this Part to accounts giving a “true and fair view” are references -

(a) in the case of Building Societies Act individual accounts, to the requirement under section 72B that such accounts give a true and fair view;

(b) in the case of Building Societies Act group accounts, to the requirement under section 73F that such accounts give a true and fair view; and

(c) in the case of IAS accounts, to the equivalent requirement under international accounting standards.”

6. (1) Section 119 of the 1986 Act (interpretation) is amended as follows.

(2) In subsection (1) -

(a) in the definition of “the annual accounts” for “section 72(10)” substitute “section 85A”.

(b) at the appropriate place insert -

““group accounts” has the meaning given by section 72E(1);”

(c) at the appropriate place insert -

““individual accounts” has the meaning given by section 72A(1);”

7. In paragraph 31(2) of Schedule 2 to the 1986 Act (members’ right to propose and circulate resolutions) -

(a) in paragraph (a)(i), for “section 72” substitute “section 72A or 72E”; and

(b) in paragraph (a)(i)(aa), for “under section 73(7)” substitute “under section 72C or 72G or in accordance with international accounting standards, as appropriate”.

STATUTORY INSTRUMENTS

2004 No.

BUILDING SOCIETIES

The Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2004

Made.....2004

Laid before Parliament2004

Coming into force2004

The Treasury, in exercise of the powers conferred upon them by sections 72C and 72G of the Building Societies Act 1986⁽⁴⁾ hereby make the following Regulations:

Citation, commencement and interpretation

1. - (1) These Regulations may be cited as the Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2004 and come into force on 31st December 2004.

(2) These Regulations apply in relation to -

(a) the annual accounts of any society, and

(b) any report which the directors of a society are obliged to prepare by virtue of section 75 of the Building Societies Act 1986,

which relates to a financial year beginning on or after 1st January 2004.

(3) In these Regulations -

(a) "the principal Regulations" means the Building Societies (Accounts and Related Provisions) Regulations 1998⁽⁵⁾; and

(b) references to numbered schedules are to Schedules to the principal Regulations.

Subsidiary undertaking with different business to be included in consolidated accounts

2. Regulation 4(7) and 4(7A) of the principal Regulations shall be deleted.

Accounts may show amounts in ECUs

3. In the principal Regulations after regulation 4, insert the following -

"Accounts in ECUs

4A.-(1) The amounts set out in the annual accounts of a society may also be shown in the same accounts translated into ECUs.

(2) Where amounts are shown in ECUs -

(a) the amounts must have been translated at the relevant exchange rate prevailing on the balance sheet date, and

⁴ 1986 c. 53 (as amended by the Companies Act 1989 and the Building Societies Act 1997)

⁵ S.I. 504/1998 (amended by S.I. 1998/248)

(b) that rate must be disclosed in the notes to the accounts.

(3) In this regulation -

“ECU” means a unit with a value equal to the value of the unit known as the ecu used in the European Monetary System, and

“relevant exchange rate” means the rate of exchange used for translating the value of the ecu for the purposes of that System.”

Alteration of heading in balance sheet formats

4. - In Schedule 2 (balance sheet formats), for “provisions for liabilities and charges”, wherever occurring, substitute “provisions for liabilities”.

(2) That expression occurs -

(a) In Part 1, under the heading “Liabilities”, in item G;

(b) In Part 2, under the heading “Liabilities”, in item G.

Alteration to which liabilities and losses to take into account

5. In Part 1 of Schedule 7 (accounting principles), in paragraph 4(1)(b) omit “and losses” and “or likely to arise”.

Amounts in accounts to have regard to the substance of the reported transaction

6. In Part 5 of Schedule 7 (other accounting rules), insert the following after paragraph 20 -

“20A. The directors of a society shall, in determining how amounts are presented within items in the income and expenditure account and balance sheet, have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice.

Inclusion of other assets at fair value

7. - (1) In Part 6A of Schedule 7 (valuation at fair value), insert the following after paragraph 31C -

Other assets which may be included at fair value

31CA.-(1) This paragraph applies to -

(a) investment property, and

(b) living animals and plants,

that under international accounting standards may be included in accounts at fair value.

(2) Such investment property and such living animals and plants may be included at fair value, provided that all such investment property, or as the case may be, all such living animals and plants are so included where their fair value can reliably be determined.

(3) In this paragraph "fair value" means fair value determined in accordance with relevant accounting standards.

(2) In Schedule 5 (notes to annual accounts), insert the following after paragraph 36 -

"Information where investment property and living animals and plants included at fair value

37.-(1) This paragraph applies where the amounts to be included in a company's accounts in respect of investment property or living animals and plants have been determined in accordance with paragraph 31CA.

(2) The balance sheet items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in a note to the accounts.

(3) In the case of investment property, for each balance sheet item affected there shall be shown, either separately in the balance sheet or in a note to the accounts -

(a) the comparable amounts determined according to the historical cost accounting rules; or

(b) the differences between those amounts and the corresponding amounts actually shown in the balance sheet in respect of that item.

(4) In sub-paragraph (3) above, references in relation to any item to the comparable amounts determined in accordance with that sub-paragraph are references to -

(a) the aggregate amount which would be required to be shown in respect of that item if the amounts to be included in respect of all the assets covered by that item were determined according to the historical cost accounting rules; and

(b) the aggregate amount of the cumulative provisions for depreciation or diminution in value which would be permitted or required in determining those amounts according to those rules."

Definition of "provisions for liabilities"

8. In Schedule 11 (interpretation of schedules) in paragraph 9(3) -

(a) for "provisions for liabilities or charges" substitute "provisions for liabilities, and

(b) for "or loss" substitute "the nature of which is clearly defined and".

Minor and consequential amendments

9. The Schedule to these Regulations makes minor and consequential amendments.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations implement in part Directive 2003/51/EC of the European Parliament and of the Council amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC as regards modernising the annual and consolidated accounts of certain types of companies, banks and other financial institutions to bring the preparation of those accounts more into line with international accounting standards (OJ L 178, 17/07/2003, p.16 - 22). A Transposition Note showing how the main provisions of this Directive (as it applies to building societies) will be transposed into UK law is available from HM Treasury (details to be inserted).

SCHEDULE

Regulation 9

1. In regulation 2 of the principal Regulations (interpretation), for "section 72", wherever occurring, substitute "section 72E".

2. (1) In regulation 4 of the principal Regulations (group accounts supplementary provisions), for "subsections (2) and (3) of section 73 of the Act", wherever occurring, substitute "subsection (2) of section 72F of the Act".

(2) That expression occurs in paragraph (3) and paragraph (12).

3. In paragraph 2 of Schedule 4 (form and content of the annual accounts of a group accounts society), for "subsections (2) and (3) of section 73 of the Act" substitute "subsection (2) of section 72F of the Act".

4. Paragraph 3 of Schedule 5 (employees in notes to annual accounts) is omitted.

5. (1) In paragraph 22 of Schedule 5 (reserves and provisions in notes to annual accounts), for "provisions for liabilities and charges", wherever occurring, substitute "provisions for liabilities".

(2) That expression occurs in sub-paragraphs (1)(b), (1)(c) and (3).

6. (1) In Schedule 6 (notes to annual accounts, information in respect of holdings in undertakings), for "subsections (2) and (3) of section 73 of the Act", wherever occurring, substitute "subsection (2) of section 72F of the Act".

(2) That expression occurs in paragraphs 3, 7, 11, 15, 18.

Draft partial Regulatory Impact Assessment on the Modernisation Directive for companies and building societies

1. Proposal

1.1 The Companies Act 1985 (International Accounting Standards and other Accounting Amendments) Regulations 2004, the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004 and the Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2004, as they implement the Modernisation Directive⁷¹

2. Purpose and intended effect

(i) Objective

2.1 The Modernisation Directive is designed to bring European accounting requirements into line with modern accounting practices. It requires Member States to make certain changes to national law concerning the form and content of company and building society accounts. It also gives Member States options on whether and how they implement certain aspects of it. This will enable companies and building societies to follow modern, more transparent accounting practices that are consistent with International Accounting Standards (IAS)

2.2 The Regulations will apply to financial years starting on or after 1 January 2005.

(ii) Devolution

2.3 Responsibility for company law matters lies with the Secretary of State for Trade and Industry, and for building society law matters with the Chancellor of the Exchequer. Company and building society law are reserved areas under the Scottish and Welsh devolution legislation and therefore any resulting changes to company and building society legislation will also apply in Scotland and Wales. In Northern Ireland, matters arising from the proposal would normally be the responsibility of the Northern Ireland Executive Ministers. Whilst the Northern Ireland Assembly and Executive are suspended, these functions will be discharged by the Northern Ireland Departments subject to the direction and control of the Secretary of State for Northern Ireland.

⁷¹ Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Council Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674 on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings. OJ L 178/16 of 17 July 2003.

(iii) Background

The Accounting Directives

2.4. EU accounting requirements are based primarily on the four Accounting Directives: the Fourth Directive on the annual accounts of certain companies⁷², the Seventh Directive on the consolidated accounts of certain companies⁷³, the Directive on the annual and consolidated accounts of banks and other financial institutions⁷⁴ (the Banks Accounts Directive), and the Directive on the annual and consolidated accounts of insurance undertakings⁷⁵ (the Insurance Accounts Directive).

The Fair Value Directive

2.5 The Fair Value Directive⁷⁶ amended the Accounting Directives to permit certain financial instruments to be recorded at fair value in accordance with IAS 39 (*Financial Instruments: Recognition and Measurement*). To deal with future developments, the Modernisation Directive gives Member States the option to extend use of the 'fair value' concept to other asset categories, and to restrict use to consolidated accounts.

The Modernisation Directive

2.6 On 6 May 2003 the Council of Ministers adopted the Modernisation Directive. This amends the Fourth and Seventh Directives on annual and consolidated accounts, the Bank Accounts Directive and the Insurance Accounts Directive.

2.7 The Modernisation Directive is designed to: -

- remove conflicts between the Accounting Directives and International Accounting Standard Board (IASB) standards in existence at the time it was drawn up; and
- ensure that optional accounting treatments currently available under IASB standards in existence at 1 May 2002 are available to EU companies and building societies which continue to have the Accounting Directives as the basis of their accounts (i.e. those companies and building societies which will not prepare their accounts in accordance with the IAS Regulation).

72 Fourth Council Directive of 25 July 1978 (78/660/EEC) based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies. OJ L222/11 of 14 August 1978.

73 Seventh Council Directive of 13 June 1983 (83/349/EEC) based on Article 54(3)(g) of the Treaty on consolidated accounts. OJ L193/1 of 18 July 1983.

74 Council Directive of 8 December 1986 (86/635/EEC) on the annual accounts and consolidated accounts of banks and other financial institutions. OJ L372/1 of 31 December 1986.

75 Council Directive of 19 December 1991 (91/674/EEC) on the annual accounts and consolidated accounts of insurance undertakings. OJ L274/7 of 31 December 1991.

76 Directive 2001/65/EC of the European Parliament and of the Council of 27 September 2001 amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions. OJ L283/28 of 27.10.2001.

2.8 The Directive must be implemented by 1 January 2005. It is not directly applicable and must be implemented through amendments to the Companies Act 1985 (“the 1985 Act”), the Building Societies Act 1986 (“the 1986 Act”) and the Building Societies (Accounts and Related Provisions) Regulations 1998 (“the 1998 Regulations”).

2.9 In a number of places, the Modernisation Directive gives Member States options on how to implement it. The Government’s general approach to implementing the Directive is to facilitate greater convergence between UK accounting standards and IAS, without imposing unnecessary burdens.

The IAS Regulation

2.10 Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of International Accounting Standards⁷⁷ introduces important changes, which will directly affect the way in which certain undertakings across the EU prepare their financial statements. Companies and building societies governed by the law of a Member State, whose securities are admitted to trading on a regulated market in any Member State in the EU (“publicly traded companies and building societies with listed securities”), will be required to prepare their consolidated accounts on the basis of accounting standards issued by the IASB that are adopted by the European Commission. It will apply to financial years commencing on or after 1 January 2005. The Government also proposes that such undertakings should be permitted to prepare their individual accounts, and all other companies and building societies should be permitted to prepare their individual and consolidated accounts, in accordance with adopted IAS.

2.11 For companies, the implementation of the IAS Regulation is being taken forward through the same Statutory Instrument as these accounting amendments. For building societies, the implementation of the IAS Regulation is being taken forward with these accounting amendments across two Statutory Instruments. In both cases, it is the subject of a separate Regulatory Impact Assessment.

Dividends

2.12 As part of the DTI consultation on implementing the Fair Value Directive⁷⁸ for companies, the Government proposed to amend the 1985 Act so that companies would no longer be required to show dividends that did not represent a liability at year-end in the profit and loss account. The proposed amendment attracted considerable comment. Many consultees did not support the amendment as proposed, and there were a number of alternative suggestions.

⁷⁷ L243/1 of 11 September 2002.

⁷⁸ Fair Value Accounting, URN 03/960, June 2003.

2.13 The Government has taken account of these comments and now proposes a revised amendment. Rather than paid and proposed dividends, companies will be required to show dividends paid (other than those for which a liability existed immediately preceding the balance sheet date) or liable to be paid. In the notes to the accounts, companies will be required to show the aggregate amount of any dividends proposed before the date of approval of the accounts, which have not otherwise been shown in the profit and loss account.

The ASB's Convergence Programme

2.14 In the UK, accounting standards issued by the Accounting Standards Board (ASB) apply to all UK companies and building societies; they are also used by a variety of other entities. The ASB and IASB standards are in many cases very similar, although there are also a number of differences. The ASB's standards will continue to apply to all UK companies and building societies and certain other reporting entities that do not report under the IAS Regulation (whether directly or by extension). The ASB does not believe it is a credible option, except in the short term, to retain two different sets of standards in use in the UK. It therefore aims to bring UK standards into line with IASB standards. It will be issuing a consultation paper shortly setting out proposals for achieving this.

Other Entities

2.15 The amendments to be made to the 1985 Act by the regulations will, unless contrary provision is made, apply automatically to Limited Liability Partnerships (LLPs) and to certain banking and insurance undertakings (including certain industrial and provident societies and friendly societies). These entities have been included in the preparation of this Regulatory Impact Assessment.

(iv) Risk Assessment

2.16 The Government is required to implement the Modernisation Directive. Failure to implement the changes required by the Directive would result in infraction proceedings being brought against the UK and would prevent companies and building societies from following up-to-date accounting requirements. Failure to implement those proposals not required by the Modernisation Directive would prevent companies and building societies from following up-to-date accounting practices.

3. Options

3.1 There are numerous permutations for implementing the provisions of the Modernisation Directive and other accounting amendments. For simplicity, only the two main overarching options of “do nothing” and full implementation are discussed.

Option 1:

Do nothing.

3.2 It is not feasible to “do nothing” for many of the accounting amendments, as that option would lead to infraction proceedings being brought against the UK for failure to implement the Modernisation Directive.

Option 2:

Implementation of the accounting amendments: to comply with the requirements to implement the Modernisation Directive; to reflect best practice in audit reporting; and to enable companies and building societies to follow up-to-date accounting practices.

3.3 Option 2 is broken in to 5 subsections a-e, which are discussed in detail below.

a. Amendments to consolidated accounts to facilitate alignment with IAS 27.

3.4 This paragraph refers to companies only. Under the existing provisions of the 1985 Act a parent company which is itself a wholly-owned subsidiary of a non-EU parent company (an intermediate parent company) is required to prepare consolidated accounts, even if electing to follow IAS and meeting the exemption criteria of IAS 27 (*Consolidated Financial Statements and Accounting for Investments in Subsidiaries*). Regulation 4 of the companies Regulations aligns the exemptions from preparation of consolidated accounts more closely with those in IAS 27 by implementing a previously unexercised Member State option in the Seventh Directive. Article 11 of the Seventh Directive gives Member States an option to exempt intermediate parent companies from the requirement to prepare consolidated accounts, if that company is a subsidiary of another undertaking not governed by the law of an EEA State, providing certain conditions are fulfilled. One of the more significant criteria is that the exempted parent must be included in a consolidation of a larger body of undertakings drawn up in accordance with the Seventh Directive or in a manner equivalent thereto. Given that the Modernisation Directive seeks to remove conflicts between the Directives and IAS, we would expect that consolidated accounts drawn up on the basis of IAS would generally meet this criterion.

3.5 Article 14 of the Seventh Directive (enacted in section 229(4) of the 1985 Act) provides for the exclusion of an undertaking from the consolidated

accounts of the parent if its activities are so incompatible with those of the parent that inclusion would fail to meet the requirement to give a true and fair view of the undertakings included therein, taken as a whole. In practice this exclusion is rarely used. This provision is in conflict with IAS 27, which does not permit any exclusion on the grounds of incompatible activities. Regulation 5 of the companies Regulations and regulation 2 of the building societies Regulations implement Article 2.6 of the Modernisation Directive by deleting Article 14 of the Seventh Directive.

3.6 Under IAS 27, an undertaking is a subsidiary undertaking if it is controlled by a parent, irrespective of the existence of an interest in the capital of the undertaking. Regulation 9 of the companies Regulations implements Article 2.1 of the Modernisation Directive by repealing the provision in section 258(4) of the 1985 Act that requires a participating interest to exist in order for an undertaking to be a subsidiary.

b. Amendments to the audit report of individual companies, building societies and groups.

3.7 Audit reports currently differ across Member States. Articles 1.15 and 1.18 of the Modernisation Directive seek to achieve greater harmonisation and reflect best practice in the format and content of audit reports. Audit reports prepared in accordance with UK Statement of Auditing Standards 600 already conform very closely to the requirements of the Modernisation Directive.

3.8 One of the changes is that, in future, the auditors will need to identify the financial reporting framework applied in the preparation of accounts (i.e. whether by IAS or UKGAAP).

3.9 Article 1.16 of the Modernisation Directive requires disclosure, whenever non-statutory accounts (eg: interim accounts) are published, of whether the auditors have drawn attention in their report to any matter by way of emphasis, without qualifying the audit report, as well as of whether the audit report was qualified or unqualified.

3.10 Regulations 6, 7 and 8 of the companies Regulations and Articles 5, 6 and 7 of the building societies Order implement Articles 1.15, 1.16 and 1.18 of the Modernisation Directive concerning the audit report of individual companies and building societies and also implement Article 2.11 concerning the audit report of groups.

c. Presentation of items within the format of accounts.

3.11 This paragraph refers to companies only. Paragraph 2 to Schedule 2 of the Regulations (and corresponding provisions in Schedules 3, 5 and 6 to the Regulations) amends paragraph 3(7) of Schedule 4 to the 1985 Act by replacing the requirement for companies to show in the profit and loss account paid and proposed dividends as separate items, with a requirement to show dividends which are paid or liable to be paid at the balance sheet

date. The amount of any proposed dividend is nonetheless important to shareholders and other users of accounts. Paragraph 3(7A) of Schedule 1 therefore introduces a new requirement for companies to disclose in the notes to the accounts the aggregate amount of dividends proposed before the date of approval of the accounts (to the extent not included in the profit and loss account).

3.12 Article 1.2 of the Modernisation Directive gives Member States the option to permit or require the presentation of amounts within items in the profit and loss account and balance sheet to have regard to the substance of the reported transaction. Paragraph 3 of Schedule 2 (and corresponding provisions in Schedules 3, 5 and 6) of the companies Regulations and regulation 6 of the building societies Regulations amend the existing requirements of the 1985 Act and the 1998 Regulations by requiring that the presentation of items within the accounting formats have regard to their economic substance.

d. Fair value of investment property, living animals and plants.

3.13 The Fair Value Directive amended the Accounting Directives to permit certain financial instruments to be recorded at fair value in accordance with IAS 39 *Financial Instruments Recognition and Measurement*. Article 1.12 of the Modernisation Directive gives Member States the option to extend the use of fair value accounting to other asset categories. Following adoption of IAS 40 *Investment Property* and IAS 41 *Agriculture* on investment property and living animals and plants the Government has decided to permit the relevant categories of assets to be fair valued in both individual and consolidated accounts. Paragraphs 6 to 8 of Schedule 2 (and corresponding provisions in Schedules 3, 5 and 6) of the companies Regulations and regulation 7 of the building societies Regulations implement this Member State option.

e. Amendments to the Directors' Report of individual building societies and groups.

3.14 Articles 1.14, 1.17 and 2.10(a) of the Modernisation Directive require directors' reports to contain a fair review of the building society's position, including an analysis of the risks and uncertainties faced, in order to give greater transparency and precision of reporting on performance on financial and non-financial matters. Articles 3 and 4 of the building societies Order implement these provisions.

3.15 The requirements relating to the directors' report in relation to companies are being taken forward with proposals for the Operating and Financial Review, which will shortly be the subject of a separate consultation and Regulatory Impact Assessment.

3.16 The Governments considers there are no risks to options 2a to e and seeks the views of consultees on the risks of these options.

4. Benefits

Option 1:

4.1 There are no benefits in choosing Option 1. To do nothing would prevent companies from following the most up-to-date accounting practices.

Option 2a to e:

4.2 Option 2a implements a Member State option in the Seventh Directive that has not previously been implemented (see paragraph 3.4 above).

This will allow the requirement to prepare consolidated accounts to be more closely aligned with IAS 27. The Government estimates that there may be some 500 companies who will benefit from these changes, with savings in accountancy staff time in not having to prepare consolidated accounts. Aligning accounting practices with IAS will increase comparability, consistency and transparency of accounts.

4.3 Option 2b makes amendments to the audit report of individual companies, building societies and groups. This will more closely align the requirements of the 1985 Act and the 1986 Act with current practice in audit reporting.

4.4 Option 2c makes amendments to the presentation of items within the format of accounts. These amendments facilitate the convergence of UK accounting standards with IAS bringing the benefits of alignment with IAS previously described. It is also important that formats do not create excessive rigidity and become an obstacle to presenting items in the most meaningful way.

4.5 Option 2d will facilitate use of up-to-date accounting practices by allowing companies and building societies to use fair value accounting for investment property and biological assets facilitating convergence with IAS.

4.6 Option 2e will facilitate greater transparency and reporting on performance on financial and non-financial matters. The directors' report will provide additional information encouraging members to exercise effective and responsible control.

4.7 The overall benefits of Options 2a to e are that they will allow company and building society law to reflect the requirements of the Modernisation Directive, reflect current best practice in audit reporting, and allow companies and building societies to follow up-to-date accounting practices.

Business Sectors Affected

4.8 There are currently approximately 1.1 million active companies on the register at Companies House and 63 building societies on the register at the Financial Services Authority. The Government estimates that Option 2a will only affect some 500 of the companies that prepare consolidated accounts. Option 2b will affect all companies and building societies that require an auditors' report. However, in practice, auditors already carry this out although not required under the 1985 Act. These changes simply reflect best practice. Option 2c will affect all companies and, where applicable, building societies, by changing the presentation of items in the format of accounts. Option 2d is optional; a company or building society in any business sector may choose to use fair value accounting for investment property and biological assets, but none will be required to do so. Option 2e will affect all building societies by introducing new requirements for the directors' report.

4.9 The proposal will particularly affect accounting firms in that they will need to take account of the change in accounting practice and train staff accordingly. There are over 64,000 UK businesses or firms operating primarily in the accounting area.

Issues of Equity and Fairness

4.10 The Department considers that the proposals will be neutral in their effect and the changes will not bring disproportionate benefits or have disproportionate effects on particular groups.

5. Costs

(i) Compliance costs

Option 1:

5.1 There would be no compliance costs on companies and building societies in the "do nothing" option.

Options 2a to e:

5.2 For Option 2a there will be a small training cost for accountants and accountancy staff and minimal IT costs. However, any costs should be outweighed overall by the benefits of time and costs saved by those companies who are able to take advantage of the exemption from having to prepare consolidated accounts.

5.3 Option 2b has minimal cost, as those requirements are a reflection of best practice already in use.

5.4 There will be a small training and IT cost to Option 2c. The amendments are not intended to make any generic changes in the presentation of specific items in the accounts. The changes will clarify the balance sheet and profit and loss formats specified by the 1985 Act and the 1986 Act by requiring that the presentation of items within the accounting formats have regard to their economic substance.

5.5 Option 2d will have a cost in the training of staff and updating of IT systems for those companies that decide to take up the fair value option. We estimate that cost to be in the region of £600 per company or building society. (1 day's training at £500 plus cost of staff time at £100).

5.6 Building societies are already required to prepare a directors' report. Option 2e will increase the costs associated with this. Costs relating to business risk assessments and identifying key performance indicators will be greater for those building societies that need to introduce systems in order to meet the new requirements. It is difficult to get a hard idea of what impact the revised audit requirement would have and what additional work auditors would carry out in order to arrive at an opinion on the consistency of the directors' report with the annual accounts. We estimate the cost of preparing a directors' report to increase by an average of £1,000, although this would vary according to the size of the building society.

5.7 The Government welcomes comments from respondents on the costs of these options.

(ii) Other costs

5.8 The Government considers that there are no costs imposed on sectors other than business. These proposals will only affect companies, LLPs and those in the banking and insurance sectors.

(iii) Costs for a typical business

5.9 For Options 2a to c there would be a minimal cost in training staff in the accountancy sector and in-house accountants, and in updating IT. Option 2d is not a requirement on businesses, but for those that choose to take it up, there will be a larger training and IT cost. However, for many businesses, it will be difficult to separate these costs from costs resulting from other accounting developments: the Fair Value Directive; increased use of IAS; and the ASB's convergence programme.

6. Consultation with small business:

The Small Firm's Impact Test

6.1 The Government considers that the proposals to implement the Modernisation Directive will have little or no cost implications for small businesses.

6.2 Small businesses have no requirements to prepare group accounts. Where they choose to prepare group accounts, it is expected that no material cost will be imposed by the proposed amendments. They are not required by the 1985 Act to have their accounts audited. Where they do so, it is expected that no material cost will be imposed by the proposed amendments. Small businesses are likely to be affected by the proposed amendments on the presentation of items within the format of accounts, but any additional cost should be minor.

6.3 The Government particularly welcomes comments on the impact of the proposal on small businesses.

7. Competition Assessment

7.1 The proposals have the potential to affect all public and private companies, building societies and LLPs in all markets. It is not anticipated that the proposal will: affect some of those businesses more than others; affect market structure; change the number or size of those businesses; lead to higher set-up costs for those businesses; or lead to higher on-going costs, than at present. The main business sector identified as being affected by this change is the accounting sector.

8. Enforcement and Sanctions

8.1 In Great Britain there is already a well-regarded enforcement regime in place for ensuring that financial statements meet the requirements of existing legislation. In addition to criminal penalties, currently the Financial Reporting Review Panel (FRRP) has legal authority to review companies' accounts and if necessary to go to court to compel a company to revise its accounts. The FRRP shares this responsibility with the Secretary of State. By administrative agreement the FRRP deals with the accounts of large public and private companies, and the Secretary of State (through Companies House) with the rest.

8.2 In terms of building societies, the 1986 Act and subsequent Regulations contain a number of requirements on accounting and auditing. Breaches of the most important of these requirements are criminal offences for which both the building society and any of its officers in default can be prosecuted

and fined. Building societies are also subject to supervision and regulation by the Financial Services Authority. The FSA receives a copy of each society's annual accounts and has a flexible range of sanctions at its disposal to ensure compliance with the statutory requirements.

9. Monitoring and Review

9.1 The EU Contact Committee on the Accounting Directives will keep the Accounting Directives under review and consider the need for further changes.

10. Consultation

(i) Within Government

10.1 The Department of Trade and Industry and HM Treasury have consulted with the Small Business Service, the Inland Revenue, Companies House, the Department for Enterprise, Trade and Industry in Northern Ireland and the Financial Services Authority.

(ii) Public consultation

10.2 In March 2004, the Department of Trade and Industry and HM Treasury published a consultation document on the Modernisation Directive/IAS Infrastructure. Approximately 800 businesses, professional bodies, representative organisations and individuals were notified of the consultation. The consultation document is available on the DTI's Internet site, and printed copies are available on request. The deadline for comments is 2 July 2004.

10.3 The Government consulted on proposals to change the requirements for companies on how dividends are shown in the accounts as part of the consultation on Fair Value in June 2003. Responses to the consultation have informed the Government's decision and are reflected in the proposals for dividends detailed at paragraphs 2.12, 2.13 and 3.11 above.

Summary and Recommendation

11.1 The table below shows a summary of the costs and benefits of the proposal:

Option	Total cost per annum	Total benefit per annum
1. "The do nothing option"	None	None
2a. Amendments to the consolidated accounts to facilitate alignment with IAS.	Minimal training and IT	Removes conflict between 1985 Act and IAS. Saving accountancy staff time.
2b. Amendments to the audit report of individual companies, building societies and groups.	Insignificant costs as changes reflect best practice currently in use.	Company and building society law will reflect best practice.
2c. Presentation of items within the format of accounts.	Small training and IT cost.	Changes will clarify the balance sheet and profit and loss formats in the 1985 Act.
2d. Fair value of investment property, living animals and plants.	£600 per company or building society cost in the training of staff, plus updating of IT systems.	Will facilitate use of up-to-date practices.
2e. Amendments to the directors' report of individual building societies and groups	£1000 per building society on average in preparing additional information for the directors' report	Greater transparency and reporting on performance on financial and non-financial matters.

11.2 The Government recommends Options 2a to e. These Options will allow company and building society law to reflect the requirements of the Modernisation Directive, reflect current best practice in audit reporting, and enable companies and building societies to follow up-to-date accounting practices.

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Draft final Regulatory Impact Assessment on the exercise of Member State Options in the International Accounting Standards (IAS) Regulation

1. Proposal

1.1 The Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004 and the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004.

2. Purpose and intended effect

(i) Objective

2.1 The objective of the proposal is to increase comparability, consistency and transparency of accounts, while keeping the burden on business to a minimum.

2.2 Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of Ministers of 19 July 2002 on the application of IAS (The “IAS Regulation”) requires publicly traded groups and other undertakings with listed securities to prepare their consolidated accounts in accordance with adopted IAS. In addition, all companies and building societies will be permitted to prepare their individual financial statements, and non-publicly traded groups and other undertakings without listed securities will be permitted to prepare their consolidated accounts, in accordance with UK Generally Accepted Accounting Practice (UKGAAP) or in accordance with IAS issued by the International Accounting Standards Board (IASB) and adopted by the European Commission.

2.3 For publicly traded companies and building societies with listed securities, adherence to adopted IAS may help to reduce the cost of capital because their accounts will be more accessible to potential investors across the EU and worldwide. For potential investors, creditors and other users of financial statements, adopted IAS will provide a consistent accounting framework to facilitate comparison of the performance and prospects of companies and building societies across the EU. For non-publicly traded companies and building societies without listed securities, adopted IAS may in some cases reduce barriers to growth by allowing them to prepare their accounts under IAS prior to application for listing.

2.4 In the UK, the Accounting Standards Board's (ASB) accounting standards apply to all companies and building societies. ASB and IASB standards are in many cases very similar, although there are also a number of differences. The ASB does not believe it is a credible option, except in the short term, to retain two different sets of accounting standards in the UK. It therefore aims to bring UK standards into line with IASB standards. Therefore, companies and building societies which choose to continue to prepare their accounts under UK GAAP may nonetheless be applying standards which are very similar to adopted IAS.

(ii) Devolution

2.5 Responsibility for company law matters lies with the Secretary of State for Trade and Industry and for building society law matters with the Chancellor of the Exchequer. Company and building society law is a reserved area under the Scottish and Welsh devolution legislation and therefore any resulting changes to company and building society legislation will also apply in Scotland and Wales. In Northern Ireland, matters arising from the proposal would normally be the responsibility of the Northern Ireland Executive Ministers. Whilst the Northern Ireland Assembly and Executive are suspended, these functions will be discharged by the Northern Ireland Departments subject to the direction and control of the Secretary of State for Northern Ireland.

(iii) Background

2.6 During 1999, the European Commission published a communication on "Financial Services: Implementing the Framework for Financial Markets: Action Plan". In March 2000, at the Lisbon European Council, Ministers of Member States concluded that, in order to accelerate completion of the internal market for financial services, steps should be taken to enhance the comparability of financial statements by 2005.

2.7 Consequently, in February 2001 the European Commission published a proposal for a Regulation on the application of IAS in the EU, as a key element of its Financial Services Action Plan. It aimed to harmonise financial reporting in the EU on the basis of globally agreed accounting standards by 2005.

2.8 The IAS Regulation was adopted on 7 June 2002. It requires publicly traded companies and other undertakings with listed securities governed by the laws of a Member State to prepare their consolidated accounts on the basis of accounting standards issued by the IASB and adopted by the European Commission, from 1 January 2005.

2.9 The IAS Regulation contains options allowing Member States to **permit** or **require**:

- publicly traded companies and other undertakings with listed securities to prepare their individual accounts in accordance with adopted IAS;
- some or all non-publicly traded companies and other undertakings without listed securities to prepare their consolidated and/or individual accounts in accordance with adopted IAS.

2.10 For companies covered by the IAS Regulation and any extension to it, adopted IAS will replace all the detailed accounting provisions of the Accounting Directives⁷⁹. These provisions have been transposed into British legislation, mostly in schedules to the Companies Act 1985 and in the Building Societies Act 1986 and regulations made under it. The effect of the IAS Regulation is that adopted IAS will be directly applicable and will have the force of law in each Member State. The IAS Regulation does not require legislative action by the Member State to transpose it into domestic law. In Great Britain it will directly supersede all the detailed accounting provisions of the Companies Act 1985 and the Building Societies Act 1986 for the companies and building societies to which the IAS Regulation applies. However, legislation is required to permit the companies and building societies to whom the Regulation is being extended the choice of using adopted IAS.

(iv) Risk Assessment

2.11 Not extending the application of the IAS Regulation, at least to some companies and building societies, could create an artificial barrier to growth. For example, non-publicly traded companies and building societies without listed securities to which the IAS Regulation did not apply might be deterred from obtaining admission to trading on a regulated market by the need to restate their past accounts to adopted IAS to provide the necessary three year record. It would also be more complicated for publicly traded parent companies and building societies with listed securities to prepare group accounts if they and their subsidiary companies were unable to prepare their individual accounts to adopted IAS.

2.12 On 10 December 2003, the Chancellor announced in his Pre-Budget Report that those companies that choose to use IAS in their individual accounts will be able to use those accounts as the starting point for their tax computations, and will not have to prepare separate UK GAAP accounts just for tax purposes. This will also apply to building societies.

3. Options

3.1 There are many permutations of the Member State options for extending the application of the IAS Regulation, from no extension, through extension to companies and building societies of certain types, size, or business sector, to full extension to all companies and building societies. These options can be either permissive or mandatory. The main options are listed below:

Option 1: No extension to the application of the IAS Regulation.

⁷⁹ The 4th and 7th Directives on the annual and consolidated accounts of companies (Directives 78/660/EEC and 83/349/EEC respectively); the Directive on the annual and consolidated accounts of insurance undertakings (Directive 91/674/EEC); and the Directive on the annual and consolidated accounts of banks and other financial institutions (Directive 86/635/EEC)

3.2 The risks of not extending the application of the IAS Regulation are discussed at paragraph 2.11 above.

Option 2(i): Extension of the application of the IAS Regulation to the individual accounts of publicly traded companies and building societies with listed securities.

3.3 It would be more complicated to prepare group accounts if the parent company or building society accounts were prepared under UK GAAP while consolidated accounts were prepared under adopted IAS.

Option 2(ii): Option 2(i) plus extension of the application of the IAS Regulation to the individual accounts of subsidiaries of publicly traded companies and building societies with listed securities.

3.4 The risks of not extending the application of the Regulation to the individual accounts of subsidiary companies are similar to those discussed for parent company and building society accounts at paragraph 3.3 above.

Option 2(iii): Extension of the application of the IAS Regulation to the individual accounts of publicly traded companies and building societies with listed securities that do not produce consolidated accounts.

3.5 Not extending the application of the Regulation to these companies and building societies may disadvantage them and hamper comparability, especially if their competitors on home or overseas markets could prepare accounts using adopted IAS.

Option 2(iv): Options 2(i) to 2(iii) plus extension of the application of the IAS Regulation to large and medium-sized non-publicly trade companies and building societies without listed securities (all companies above those small companies that could apply the ASB's Financial Reporting Standard for Smaller Entities (FRSSE) and equivalent sized building societies).

3.6 A two-tier accountancy profession already exists where accountants dealing with medium, large and listed businesses have the specialist knowledge to prepare complex accounts, while accountants working with small businesses are more used to dealing with simple accounts. This option may have the unintended consequence of exacerbating this split.

Option 2(v): Extension of the application of the IAS Regulation to all companies and building societies.

3.7 If this option was pursued on a mandatory rather than permissive basis, it could increase the burden on small companies and building societies. IAS has many reporting requirements that are more suitable for larger businesses, and there is currently no international equivalent of the ASB's reporting standard for small companies (the FRSSE).

Option 2(vi): Sector specific option: Extension of the application of the IAS Regulation to companies and building societies prudentially regulated under the Financial Services and Markets Act 2000.

3.8 Extending only to this particular sector may disadvantage other businesses and hamper comparability if their competitors on home or overseas markets could prepare accounts to adopted IAS.

4. Benefits

Option 1:

4.1 The benefit to business in not extending application of the IAS Regulation is that no cost burden will fall on companies and building societies other than those who will be required by the IAS Regulation to use adopted IAS in the preparation of their consolidated financial statements.

Options 2(i), 2(ii), 2(iii), 2(iv), 2(iv) and 2(vi):

4.2 A benefit of extension generally is that for companies and building societies that do business or seek capital across borders compliance with adopted IAS would make their accounts more comparable with those of their competitors in IAS countries. This comparability would assist shareholders, analysts and other users of accounts. There could also be cost savings as a result of not having to prepare different accounts according to different national standards.

4.3 A benefit of extension for options 2(i) and (2ii) is that groups of companies and building societies would not have to prepare their accounts using two accounting methods. Both individual and consolidated accounts and would be prepared in accordance with adopted IAS.

4.4 A benefit of extension for option 2(v) is that it would not create a barrier to growth, in that small companies and building societies would not be faced with the need to change their accounting systems completely when they got above a certain size. If implemented on a mandatory basis, it would also provide full comparability of all accounts. There would be a single set of accounting standards, which would have the advantages of simplicity, certainty and transparency.

4.5 Extension on a permissive rather than mandatory basis for any of the options has the benefit of minimising burdens on business. There will be costs for a company and building society in switching to IAS. A permissive approach would mean that companies and building societies can switch to IAS when it best suits their own circumstances, and when they judge that the benefits outweigh the costs.

4.6 When consulting on the options⁸⁰ we requested that respondents consider the costing of benefits to using adopted IAS and provide estimates as to these benefits. Those respondents who commented on the benefits were not able to quantify them.

Business Sectors Affected

4.7 This proposal will potentially affect all companies and building societies in Great Britain. There are currently approximately 1.1 million active companies on the register at Companies House and 63 building societies on the register at the Financial Services Authority. It is not possible to say how many of these will choose to prepare their accounting in accordance with adopted IAS.

Issues of Equity and Fairness

4.8 The Government considers that the proposal will not bring disproportionate benefits or have disproportionate effects on particular groups.

5. Costs

(i) Compliance costs

Option 1:

5.1 If the application of the IAS Regulation is not extended, there will be no cost to businesses other than that falling on those already covered by the IAS Regulation. Any cost on shareholders, analysts and other users of accounts (such as investors, creditors and enforcement bodies) of having to be familiar with two sets of accounting regimes for investment or compliance purposes arises from the IAS Regulation itself rather than any extension to it.

80 International Accounting Standards, a consultation document on the possible extension of the European Regulation on International Accounting Standards, 30 August 2002, DTI, URN 02/1158

Options 2(i) & 2(ii) (Extension of the application of the IAS Regulation to the individual accounts of publicly traded companies and building societies with listed securities and to the individual accounts of their subsidiaries) – on a mandatory basis:

5.2 The additional cost of extending the application of the IAS Regulation to the individual accounts of publicly traded companies and building societies with listed securities and the individual accounts of subsidiaries should be minimal. These companies would need to prepare underlying accounting data in accordance with adopted IAS in order for the parent company or building society to prepare the group accounts already covered by the IAS Regulation.

5.3 Our best estimate is that for these categories of company and building society, a decision to prepare accounts in accordance with adopted IAS could be broadly neutral in cost terms. Groups whose parent company is publicly traded or whose parent building society has listed securities would incur ongoing costs in maintaining capability in two different accounting frameworks if they were unable to use adopted IAS in their individual and subsidiary accounts. However, switching to adopted IAS for these accounts would also require a one-off investment to restate comparative figures, re-design systems and procedures and adapt to different disclosure requirements. Also, some ongoing costs might arise as a result of adopted IAS's different requirements for subsidiary companies (e.g. the requirement to prepare a cash flow statement for each subsidiary).

Options 2(iii), 2(iv), 2(v) & 2(vi) (Extension of the application of the IAS Regulation to all companies and building societies excepting Options 2(i) and 2(ii)) – on a mandatory basis:

5.4 There will be a one-off cost for companies and building societies choosing to comply with the IAS Regulation. Companies and building societies will have to change the basis on which they prepare their accounts, entailing changes to accounting systems. Changes to IT systems would be required, but we do not currently have estimates for these.

5.5 There will be one-off training costs for staff in being instructed in the standards and in interrogating the data in order to compile accounts to a different accounting regime. Anecdotal evidence suggests that small companies and building societies may require 1 person to be trained for 2 days. Medium to large companies and building societies may require 2 staff to be trained for between 3 and 5 days. This gives the following estimates:

Cost of training course	£750 per day (cost of a one day training package on IAS)
Cost of staff time per day	£100 per day (assuming staff pay of £25,000 per annum approximately)

5.6 We estimate the training costs for small companies may be approximately £1,700 per business (or £1,467m ((£750 x 2 + £100 x 2) x 863,000) for the sector as a whole). It is possible that as many as 60% of small businesses may not have in-house accountancy staff and therefore would not incur a training cost. This would reduce the one-off cost burden on this sector to £587m. However, in these cases there may be a need for additional external advice and support. We do not have estimates for their potential cost. It is estimated that the cost for medium to large companies and building societies may be between £5,100 and £8,500 per business (or between £1,280m (2 x £750 x 3 + 2 x £100 x 3) x 251,000) and £2,134m ((2 x £750 x 5 + 2 x £100 x 5) x 251,000) for the sector as a whole).

5.7 There may be additional on-going costs for small companies and building societies in having to comply with adopted IAS. IASB standards are primarily focused on the reporting requirements of large publicly traded companies, which are involved in complex transactions. Some standards are arguably less relevant to small businesses or require them to account for certain transactions in overly complex ways. As yet, there is no equivalent IASB to the ASB's FRSSE, which brings together in one place, with some simplifications, the accounting requirements from each of the full domestic standards as they apply to small businesses.

5.8 We would estimate the extra staff time spent in applying adopted IAS to small companies or building societies to be in the region of 1 person for 2 days per annum. Assuming the cost of staff time to be approximately £100 per day (a salary of £25,000 per annum), the cost of this may be approximately £200 per business (or £172.6m (£100 x 2 x 863,000) for the sector as a whole). Again, if as many as 60% of small businesses do not prepare their own accounts, the on-going cost burden would be reduced to £69m for the sector as a whole. However, once again additional cost may be incurred in respect of external advice and support.

5.9 There will also be costs for accountancy firms in a mandatory change to IAS. There are some 64,000 accountancy businesses or firms in the UK. We estimate there will be one-off training costs for two days training for a partner and 2 others in the region of £5,700 (or £365m for the sector as a whole), broken down as follows:

Cost of training course	£750 per day (cost of a one day training package on IAS)
Cost of staff time per day	£100 per day (assuming staff pay of £25,000 per annum approximately)
Cost of partner time £400	(assuming partner pay of £100,000 per annum approximately)

Options 2(v) (Extension of the application of the IAS Regulation to all companies) – on a permissive basis

5.10 If companies and building societies are required to adopt IAS in the preparation of their financial statements compliance costs will be incurred. **Permitting** companies and building societies to use adopted IAS will impose no compliance costs. Giving companies and building societies the ability to choose to use adopted IAS in the preparation of their accounts will allow them the flexibility to prepare accounts in accordance with the accounting framework that is best suited to their needs. They will choose to switch to adopted IAS when they judge that the benefits outweigh the costs. There will be a cost to those accountancy firms dealing with publicly traded groups or building societies with listed securities, arising directly from the IAS Regulation. There will be a cost on other accountancy firms in permitting non-publicly traded companies and building societies without listed securities to use adopted IAS. Those firms will need to become familiar with IAS in order to advise their clients on whether to switch. However, the ASB's convergence programme will mean that IAS and UK GAAP are similar, thereby reducing the cost of becoming familiar with IAS.

5.11 When consulting on the options for companies, we requested that respondents consider the cost of using adopted IAS and provide estimates as to the costs. Those respondents who commented on costs said that it was difficult to quantify those costs. The estimates provided varied widely and are summarised below:

- Mandatory extension of IAS will cost small companies an estimated £150 pa.
- Implementation costs likely to exceed £0.5m for the group on whose behalf the respondent answered.
- Consultancy costs are over £1,000 per day and significant assistance will be required.
- Costs of installation and training could be between £200 and £500 per company.
- Costs of Finance function in a large limited company likely to rise by some 10% (£25,000) pa.
- Costs of audit in a large limited company likely to rise by some 10% (£5,000) pa.

(ii) Other costs

5.12 The DTI considers that there are no costs imposed on sectors other than business.

(iii) Costs for a typical business

5.13 The costs for a typical business are discussed in detail at paragraphs 5.4 to 5.10 above.

6. Consultation with small business:

The Small Firm's Impact Test

Stage 1

6.1 Our estimates at paragraphs 5.5 and 5.6 above show that there may be a one-off training cost of £1,700 for a small company should it choose to use adopted IAS in the preparation of its financial statements. It is possible that as many as 60% of small companies may not have in-house accountancy staff and therefore would not incur a training cost. There will be no cost to small companies if they choose not to use adopted IAS.

Stage 2

6.2 The consultation document and its small firms summary was made widely available. The Small Practitioners Association (SPA), who represent an independent group of small professional practices serving a total of some 90,000 incorporated businesses (the vast majority of which are small) were not in favour of compulsory extension to small companies. The SPA felt there would be little impact on small companies, as few would choose to move to adopt IAS.

6.3 The London Society of Chartered Accountants (with a membership of 30,000) commented that the application of adopted IAS should be extended to all companies on either a voluntary or compulsory basis, dependent on the options. However, the IAS regulation should not be applied to the accounts of small companies (as defined) in the short term until a FRSSE has been developed that is consistent with IAS.

6.4 The Government encouraged several other small business organisations to respond to the consultation but did not receive comments.

7. Competition Assessment

7.1 The proposal has the potential to affect all companies and building societies that choose to prepare their financial statements in accordance with adopted IAS. It is not anticipated that the proposal will: affect some of those businesses more than others; affect market structure; change the number or size of those businesses; lead to higher set-up costs for those businesses; or lead to higher on-going costs, than at present.

7.2 The main business sector identified as being affected by this change is the accounting sector.

8. Enforcement and Sanctions

8.1 In Great Britain there is already a well-regarded enforcement regime in place for ensuring that financial statements meet the requirements of existing

legislation. Currently the Financial Reporting Review Panel (FRRP) has legal authority to review companies' accounts and if necessary to go to court to compel a company to revise its accounts. The FRRP shares this responsibility with the Secretary of State. By administrative agreement the FRRP deals with the accounts of large public and private companies, and the Secretary of State (through Companies House) with the rest.

8.2 In terms of building societies, the Building Societies Act 1986 and subsequent Regulations contain a number of requirements on accounting and auditing. Breaches of the most important of these requirements are criminal offences for which both the building society and any of its officers in default can be prosecuted and fined. Building societies are also subject to supervision and regulation by the Financial Services Authority. The FSA receives a copy of each society's annual accounts and has a flexible range of sanctions at its disposal to ensure compliance with the statutory requirements.

9. Monitoring and Review

9.1 The Government proposes to review the adoption of the IAS Regulation around 2008 and re-evaluate the extension options having regard to developments in the ASB's convergence programme and the IASB's development of an International FRSSE.

10. Consultation

(i) Within Government

10.1 The Department of Trade and Industry and HM Treasury have consulted with the Inland Revenue, The Financial Services Authority, the Small Business Service, Companies House and the Department for Enterprise, Trade and Industry in Northern Ireland.

(ii) Public consultation

10.2 On 2 September 2002, the Department published a consultation document on the possible extension of the IAS Regulation to companies. The consultation was sent to approximately 1,000 businesses, professional bodies, and representative organisations and individuals, and was also made available on the internet. The consultation closed on 26 November 2002. 69 responses were received.

10.3 In March 2004, the Department of Trade and Industry and HM Treasury published a consultation document on the Modernisation Directive/IAS Infrastructure. Approximately 800 businesses, professional bodies, representative organisations and individuals were notified of the consultation. The consultation document is available on the DTI's Internet site, and printed copies are available on request. The deadline for comments is 2 July 2004.

11. Summary and Recommendation

11.1 The table below shows a summary of the costs and benefits of the proposal:

	Approximate number of companies and building societies affected	Cost of mandatory extension of the IAS Regulation (£)	Cost of voluntary extension of the IAS Regulation (£)	Benefit (£)
Option 1	N/A	N/A	N/A	N/A
Option 2 (i)	2,700	Minimal	NIL	Not having to prepare group accounts using different sets of accounting standards
Option 2 (ii)	27,000	NIL	NIL	Not having to prepare group accounts using different sets of accounting standards
Option 2 (iii)	250	£2.1m approx in one-off training costs. There will be one-off IT system costs, which have not yet been estimated.	NIL	Easier comparison across sectors and markets.
Option 2 (iv)	75,000	Between £1,280m and £2.134m approx in one-off training costs. There will be one-off IT system costs, which have not yet been estimated.	NIL	Easier to seek admission to trading on a regulated market. Easier comparison across sectors and markets.
Option 2 (v)	1,100,000	Between £1,867m and £3,601m in one-off training costs. Between £69m and £172.6m in on-going compliance costs. There will be one-off IT system costs, which have not yet been estimated. Costs to accountancy sector £365m.	NIL	Easier comparison across sectors and markets.
Option 2 (vi)	This option has not been costed because of the difficulty in identifying the number of companies covered	NIL		

11.2 The DTI recommends option 2(v) on a voluntary basis. The benefits of this option are:

- Parent companies and building societies and subsidiaries in groups will be able to prepare their accounts to one framework of accounting standards.
- Companies and building societies that do business or seek capital across borders would be able to prepare their accounts to adopted IAS for ease of comparison.
- Comparability of accounts will assist, shareholders, analysts and other users of accounts.
- Comparability of accounts will help maintain the attractiveness of British companies and building societies to international investors.
- Costs savings in not having to prepare accounts to different national standards.
- Companies and building societies of different sizes will be able to choose which standard is best suited for their needs.

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ANNEX G

Code of practice on written consultations

The following criteria apply to all UK national public consultations, and have been applied to this consultation paper.

- 1.** Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
- 2.** It should be clear who is being consulted, about what questions, in what timescale and for what purpose.
- 3.** A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
- 4.** Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others), and effectively drawn to the attention of all interested groups and individuals.
- 5.** Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
- 6.** Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and reasons for decisions finally taken.
- 7.** Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated.

Responses to the consultation should be sent to the address given at paragraph 2.2 of the consultation document. If, however, you wish to make any comments about the handling of this consultation, please contact:

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Further information about this code of practice can be found at: www.cabinet-office.gov.uk/servicefirst/index/Consultation.htm.