

Consultation on EC directives:

2006/43/EC - Statutory Audit Directive

2006/46/EC - Amending the Accounting Directives

January 2008



HM TREASURY



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2006/46/EC - Amending the
Accounting Directives**

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If you require this information in another language, format or have general enquiries about HM Treasury and its work, contact:

Correspondence and Enquiry Unit
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 4558

Fax: 020 7270 4861

E-mail: public.enquiries@hm-treasury.gov.uk

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EXECUTIVE SUMMARY

This consultation document sets out HM Treasury's proposals for implementing the following EC Directives in relation to building societies and friendly societies:

- Directive 2006/43/EC on the statutory audits of annual accounts and consolidated accounts; and
- Directive 2006/46/EC on the annual and (consolidated) accounts of certain types of companies (banks, other financial institutions and insurance undertakings).

Together the two Directives seek to improve the credibility of financial statements provided by businesses in the EU, establish some basic sets of principles for the conduct of statutory audits and to engender good corporate governance practice.

The provisions of the Directives affect statutory auditors, audit firms and with the exception of specific optional exemptions, to audits of all entities already required to have an audit of annual accounts or consolidated accounts under Community Law. This includes companies, credit institutions (i.e. banks and building societies) and insurance undertakings, which may be companies, friendly societies or industrial & provident societies.

The Department for Business Enterprise and Regulatory Reform (BERR) has conducted consultations on the impact of the two Directives on companies. This consultation is therefore specifically aimed at the mutual societies for which the Treasury has policy responsibility (i.e. building societies and friendly societies). BERR are implementing the provisions of the Directives in relation to Industrial & Provident Society Insurers, which are within scope of the Directives.

This consultation document should be read in conjunction with the

- Draft Statutory Instruments ("the SIs") at Chapter 3
- Draft Impact Assessments ("the IAs") at Chapter 4; and
- Directives 2006/43/EC and Directives 2006/46/EC ("the Directives") obtainable from www.europa.eu.int.

The Government proposes to implement these Directives in an effective, proportionate, risk-based manner and would welcome your comments on the likely costs, benefits and implications of implementing these proposals as set out in the draft Impact Assessment and Statutory Instruments.

Comments you may have on reducing any associated real or perceived regulatory burdens and any specific comments on issues that might need to be addressed to reflect any different legal and regulatory frameworks across England, Wales, Scotland and Northern Ireland would also be particularly welcome.

This consultation will be open for 8 weeks from 4th January 2008 to 29 February 2008. Please ensure we have your response by the deadline.

INTRODUCTION

Directive 2006/43/EC on the Statutory Audits of annual accounts and consolidated accounts (8th Company Law Directive).

Directive 2006/46/EC on Amending EC Accounting Directives (4th and 7th Company Law Directives).

Background 1.1 One of the European Commission's aims is to modernise company law and enhance corporate governance in the European Community. The Commission's Action Plan adopted on 21 May 2003 included a short-term aim which sought Member States to confirm the collective responsibility of board members, increase transparency in transactions with related parties, off-balance sheet arrangements and improve disclosure about corporate governance practices applied in companies. The ensuing Directives discussed below are a result of this plan.

Directive 2006/43/EC – Statutory Audit Directive

1.2 Directive 2006/43/EC was adopted on 17 May 2006 and published in the Official Journal of the European Communities on 9 June 2006. The purpose of this Directive was “to improve the credibility of financial information and to strengthen protection in the European Union against financial scandals”. In addition, the Directive sought to establish a set of basic principles for the conduct and oversight of statutory audits conducted in the European Union. The full text of the Directive can be found at www.europa.eu.int. The deadline for implementing this Directive is 29 June 2008 however both BERR and HM Treasury are aiming to implement the majority of provisions on the common commencement date of 6th April 2008.

1.3 Directive 2006/43/EC clarifies the duties of statutory auditors and provides for their independence and ethical standards; introduces a requirement for external quality assurance; provides for public oversight of the audit profession, including third country auditors and improved cooperation between oversight bodies in the EU. It also provides a basis for international cooperation between regulators in the EU and with regulators in third countries, such as the US Public Company Accounting Oversight Board (PCAOB).

1.4 The Department for Business Enterprise & Regulatory Reform (BERR) published a consultation document on implementing options for Directive 2006/43 (in relation to companies). The consultation commenced on 5 March 2007, and closed on 1 June 2007. Following on from this BERR published the Government's conclusions and a set of draft regulations on 19 July 2007 with a request for comments and supporting evidence by 15 October 2007. The Statutory Auditors and Third Country Auditors Regulations 2007 (SI 2007/3494) were made on 17 December. At the same time BERR also published a summary of responses and Government response to its consultation on the draft regulations. The final regulations and an Explanatory Memorandum, Impact Assessment and Transposition Note are available at www.opsi.gov.uk/si/si200734 while all the consultation material published during 2007 is available at BERR's website at <http://www.berr.gov.uk>

Directive 2006/46/EC – 4th and 7th Company Law (Accounting) Directives

1.5 Directive 2006/46/EC of the European Parliament and of the Council on Company Reporting was published in the Official Journal of the European Commission on 16 August 2006. The purpose of this Directive was to “further enhance confidence in the financial statements and annual reports published by European companies to provide shareholders and other stakeholders (e.g. employees and suppliers) with reliable complete and easily accessible information”. It amends Council Directives

- 78/660/EEC on the annual accounts of certain types of companies (“the 4th Directive”);
- 83/349/EEC on consolidated accounts (“the 7th Directive”);
- 86/635/EEC on the annual and consolidated accounts of banks and other financial institutions (“the Bank Accounts Directive”); and
- 91/674/EEC on the annual accounts and consolidated accounts of insurance undertakings (“the

The full text of the Directive can be found at www.europa.eu.int. The deadline for Member States to implement Directive 2006/46/EC is 5 September 2008 however both BERR and HM Treasury are aiming to do this on the common commencement date of 6th April 2008.

1.6 BERR published a consultation on the implementation for the measures in Directive 2006/46 (as they apply to certain companies) on 5 March 2007. The consultation closed on 1 June 2007 and the Government published a summary of responses and its conclusions, and issued draft regulations for comment in July. The regulations were laid in Parliament on 17 December. The regulations and an Explanatory Memorandum, Impact Assessment and Transposition Note are available at <http://www.opsi.gov.uk/si/dsis2007.htm>, while the consultation material is available at www.berr.gov.uk/consultations/closedwithresponse/index.html.

Who is affected?

1.7 The two EC Directives will affect companies, certain partnerships, building societies, those friendly societies and industrial & provident societies covered by the Insurance Accounts Directive, and other institutions covered by the Bank Accounts Directive. The changes will apply in relation to financial years commencing on or after 6 April 2008.

Devolution

1.8 **Building societies** in the UK are governed by the Building Societies Act 1986 (BS Act 1986) and regulated by the Financial Services Authority (FSA). Building society law is reserved to Westminster under the Scottish, Welsh and Northern Irish devolution legislation. All the provisions of the two implementing statutory instruments for building societies will therefore apply to the whole of the UK.

1.9 **Friendly societies** are registered under the Friendly Societies Act 1974 or incorporated under the Friendly Societies Act 1992 and are regulated by the Financial Services Authority. The provisions of the Directive will be implemented on a UK-wide basis.

1.10 The draft Statutory Instrument the Treasury is consulting on do not make any changes in relation to Industrial & Provident Societies. Those will be made in the Statutory Instruments being produced by BERR.

Policy Responsibility **1.11** HM Treasury (HMT) has policy responsibility for the legislative and regulatory framework for the mutual sector whilst BERR has responsibility for that relating to companies and partnerships.

1.12 As noted above the BERR has already held public consultations on the two Directives (2006/43 and 2006/46) in as far as they relate to companies. HMT is now holding a parallel consultation on these Directives in relation to mutual societies (specifically building societies and friendly societies). The Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008 will implement the Directive for other insurers, including Industrial and Provident Society insurers. These Regulations will be made by BERR and are published on their website at www.berr.gov.uk

1.13 HMT will be working closely with BERR on their implementation for companies and the two Departments aim to implement the Directives for all the entities affected (companies, building societies, friendly societies and other affected bodies) simultaneously. For building societies and friendly societies, the Treasury proposes to implement the Directives using powers in the Building Societies Act 1986 and the Friendly Societies Act 1992, as well as using section 2(2) of the European Communities Act 1972. Both Departments propose for the provisions to come into force for reporting periods on or after 6 April 2007.

How to respond **1.14** This consultation document will be sent to the representative bodies of building societies, friendly societies, academics, and other stakeholders including the accounting bodies. It will also be posted on the Treasury public website and printed copies will be available on request.

1.15 This consultation will last 8 weeks from 4th January 2008 to 29th February 2008. Please send your responses to:

Samuel Amissah

Room 3/20

Savings & Investment Team

International & Finance Directorate

HM Treasury

1 Horse Guards Road

London SW1 2HQ

Disclosure of responses **1.16** When responding, please state if you are responding as an individual or representing the views of an organisation. In accordance with the code of practice on open government, comments will be made publicly available unless respondents specifically request otherwise. In the case of electronic responses, general confidentiality disclaimers that often appear at the bottom of e-mails will be disregarded for the purpose of publishing responses unless an explicit request for confidentiality is made in the body of the response. If you wish part, but not all, of your response to remain confidential please supply two versions- one for publication on the website with the confidential information deleted and another confidential version for the HMT consultation team.

Impact Assessment

1.17 HM Treasury has prepared partial Impact Assessments looking at the potential costs and benefits of the proposed measures. A full impact assessment will be published in due course after consultation responses have been received and analysed.

Confidentiality Disclosures

1.18 Information provided in response to this consultation, including personal information, might be published or disclosed in accordance with the access to information regime. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

1.19 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, among other things, with obligations of confidence. In view of this it would be helpful if you could tell us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take account of your explanation, but we cannot give an assurance that confidentiality will be maintained in all circumstances.

1.20 An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department. Your personal data will be processed in accordance with the DPA, and in the majority of circumstances, this will mean that your personal data will not be disclosed to third parties.

Freedom of Information contact

1.21 Any Freedom of Information Act queries should be directed to:

Correspondence and Enquiry Unit

Freedom of Information Section

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

Telephone: +44 (0) 20 7270 4558

Fax: +44 (0) 207 270 4681

Email: public.enquiries@hm-treasury.x.gsi.gov.uk

Cabinet Office code of practice

1.22 The Cabinet Office has published a Code of Practice for Written Consultations to guide Department's activities in this area, which sets out the following criteria:

- consult widely throughout the process, allowing a minimum of 12 weeks for written consultations at least once during the development of the policy;

- be clear about what the proposals are, who may be affected, what questions are being asked, and what timescales for responses;
- ensure the consultation is clear, concise and widely accessible;
- give feedback regarding the responses received and how the consultation process influenced the policy;
- monitor the department's effectiveness at consultation, including through the use of a designated consultation co-ordinator; and
- ensure your consultation follows better regulation best practice, including carrying out an Impact Assessment if appropriate.

1.23 This consultation will last for 8 weeks. The detailed provisions of the Directives have already been fully consulted on by BERR with respect to companies, the main entities, affected by the two Directives. The two EC Directives are mandatory and HM Treasury is merely giving mutual societies who will be affected advance notice of the implementation and the opportunity to air their comments on the proposed approach.

1.24 If you feel that this consultation does not fulfil these criteria, please contact:

Sowdamini Kadambari

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

Tel: 020 7270 4867

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KEY POLICY ISSUES

2.1 This chapter discusses some of the relevant policy issues in the Directives and the Treasury's implementation proposals in relation to the mutual societies affected.

2.2 As explained in Chapter 1, BERR is responsible for implementing the Directives in relation to companies. Some of this implementation will be covered by parts of the Companies Act 2006, which come into force in April 2008. BERR have also published draft Regulations, alongside their consultation documents, which will implement other provisions of the Directives. Further provisions will be implemented by Financial Services Authority (FSA) rules and regulations made by the Professional Oversight Board (POB). Full details are given in the BERR consultation documents and responses.

2.3 The HMT implementation strategy for this Directive will seek where appropriate to mirror closely the approach taken by BERR in the implementation of the proposals in relation to companies. It is the Government's view that this approach, which is intended to build on the existing audit framework, will minimise any new burdens on business. Some of BERR's and FSA's implementation will automatically cover building societies and friendly societies.

2.4 In particular, Part 42 of the Companies Act 2006, which concerns statutory auditors, will apply in relation to audits of building societies and those friendly societies within the scope of the Directive when it comes into force in April 2008. Also, FSA listing rules apply to all entities, which issue securities, which are traded on a regulated market in the UK, including any building societies or friendly societies, which issue such securities.

2.5 Other provisions of the Directive will need specific implementation for building societies and friendly societies. This is explained more fully below.

2.6 The provisions and Directive requirements will affect all UK building societies, and those friendly societies and Industrial & Provident Societies covered by the insurance Directive.

1. Do you have any comments on the:

(a). Government's overall approach for implementing the requirements of the Directives in relation to building societies and friendly societies.

(b). Draft Impact Assessments and Statutory Instruments?

(c). Likely costs and benefits or implications of implementing the proposals as set out in the draft Impact Assessments and Statutory Instruments.

2. Do you foresee any additional regulatory burdens on the affected entities as a result of these Directives and if so how can these be mitigated?

Directive 2006/43/EC

2.7 The overall objective of this Directive is to clarify the duties of statutory auditors in Member States and to provide for their independence and ethical standards. It also introduces a requirement for external quality assurance; provides for public oversight of the audit profession, including third country auditors and improved cooperation between oversight bodies in the EU.

2.8 Unlike in some Member States, the existing UK framework for statutory audits of entities already provides for a significant proportion of the areas covered by the Directive. Thus in the most part the Directive only requires minor adjustments to pre-existing UK legislation and regulatory practice to ensure compliance. There are however some new provisions which need to be implemented.

2.9 The Government's view is that BERR and/or FSA's proposed implementation of the following provisions of the Directive will be effective for building societies and friendly societies without the need for further specific implementation:

- Education and qualifications (Articles 3 to 14, and 44)
- Registration (Articles 15 to 20)
- Ethics (Articles 21 to 25)
- Standards and reporting (Articles 26 and 27(b) and (c));
- Public oversight, investigations and discipline (Articles 29 to 36)
- Public interest entities (Articles 39 to 43);
- Third country auditors (Articles 45 to 46);
- Co-operation with third country authorities (Article 47).

2.10 This consultation document does not therefore discuss these provisions any further. For details of the Government's proposed implementation of these provisions, please refer to the BERR consultation document and response.

3. Do you have any comments on these provisions as they apply to building societies and friendly societies?

Statutory audits of consolidated accounts

2.11 Article 27 of the Directive sets out provisions for the statutory audits of consolidated accounts of a group of undertakings. Article 27(a) requires that the group auditor bears the full responsibility for the audit report in relation to consolidated accounts. This requirement is already provided for in relation to companies by section 495 of the Companies Act 2006.

2.12 The Government is satisfied that this requirement is already provided for in relation to building societies (by section 78(4)(c) of the Building Societies Act 1986) and friendly societies (section 73 of the Friendly Societies Act 1992). Therefore no further action is required.

4. Do you have any comments in relation to Article 27(a) on the statutory audits of consolidated accounts?

Audit reporting

2.13 Article 28.1 on audit reporting requires the statutory auditor to sign the audit report and allows Member States to provide that the name of this person need not be disclosed to the public for security reasons.

2.14 For companies this is implemented by ss. 503-506 of the Companies Act 2006. For Building Societies and Friendly Societies there is already a requirement for the auditors to sign the report, but (in contrast to companies) there is no requirement for the auditor to sign in his own name (rather than the name of the firm), and there is no provision for the exception referred to earlier. The position for Building Societies and Friendly Societies is the same as it was for companies before the Companies Act 2006.

2.15 HMT is proposing to amend the relevant provisions of the Building Societies and Friendly Societies Acts to bring them into line with Companies Act on this point.

2.16 Article 5 of the draft Building Societies Act 1986 (Accounts, Audit and EEA State Amendments) Order 2008 (“the Building Societies Act Order”) substitutes new sections 78A to 78D in the Building Societies Act 1986 Act in place of the current s.78A. These are based on sections 503-506 of the Companies Act 2006. Article 5 of the draft Friendly Societies Act 1992 (Accounts, Audit and EEA State Amendments) Order (“the Friendly Societies Act Order”) makes similar amendments, substituting new sections 74 to 74C for section 74 of the Friendly Societies Act 1992.

2.17 These amendments are made using the powers in the Building Societies Act 1986 and the Friendly Societies Act 1992 to assimilate certain provisions in those Acts to company law (section 104 of the 1986 Act and section 102 of the 1992 Act).

2.18 A new offence is created under these provisions. If a building society or friendly society sends a copy of its auditor’s report to the Financial Services Authority, or otherwise publishes it, without stating either the name of the auditor or that the society has resolved to omit the auditor’s name for security reasons, it commits an offence. Every officer of the society who is in default also commits an offence. The penalty is a fine not exceeding level 3 (currently £1,000) on summary conviction. (See new section 78C of the Building Societies Act 1986 and new section 74B of the Friendly Societies Act 1992). These replace the existing offences in section 78A of the 1986 Act and section 74 of the 1992 Act. The offences, and the penalties, are the same as the equivalent offence in relation to companies (see s.505 of the Companies Act 2006).

2.19 There are however some differences from the equivalent company law provisions. A building society or a friendly may omit the name of its auditor from copies of the auditor’s report sent to the Financial Services Authority (under the relevant Act) or otherwise published, if publishing the name would create a security risk for the auditor or any other person. To do so it must pass a members’ resolution and notify the Authority of the resolution. The equivalent resolution for a company must be notified to the Secretary of State (s.506 Companies Act 2006).

2.20 The reason for this difference is that the Financial Services Authority performs all registrar and executive-type functions in relation to building societies and friendly societies – the Government and its agencies have no role. It should also be noted that the copy of the auditor’s report sent to the Authority under the relevant Act must be

placed on the public file of the society, but a resolution to omit the name would not be placed on the public file.

2.21 There are further differences in relation to friendly societies, as not all friendly societies covered by the 1992 Act are within the scope of the Directive. If a friendly society does not appoint a statutory auditor as defined in Part 42 of the Companies Act 2006, the auditor's report will, as at present, be signed in the name of the audit firm. Only friendly societies, which are within the scope of the Insurance Directive, will appoint statutory auditors (see s.1210 Companies Act 2006).

2.22 The draft Friendly Societies Act Order applies the provisions on omitting the auditor's name from the report to all friendly societies, which carry on insurance business, whether or not they are within the scope of the Insurance Directive. This is considered to be a useful reform.

5. Do you have any comments on the Government's proposed implementation of Article 28.1 for building societies and friendly societies?

6. Do you agree that a resolution to omit the auditor's name from the audit report should be notified to the Financial Services Authority?

7. Do you agree that the provisions on omitting the auditor's name should be extended to non-Directive friendly societies?

8. Do you agree that the offence of failing to state an auditor's name (or that a resolution has been passed to omit the name) and the proposed penalty are appropriate?

Appointment of auditors

2.23 Article 37.1 of the Directive requires the statutory auditor or audit firm to be appointed by the general meeting of shareholders or members of the audited entity. Member States may provide for alternative appointment methods provided that the independence of the auditors is not compromised.

2.24 This provision is already met in relation to companies by Part 16 of the Companies Act 2006. It is also met in relation to building societies by section 77 of, and Schedule 11 to, the Building Societies Act 1986, and in relation to friendly societies by section 72 of, and Schedule 14 to, the Friendly Societies Act 1992. So no further implementation is necessary in relation to building societies or friendly societies.

9. Do you have any comments in relation to Article 37.1 of the Directive?

Dismissal and resignation of auditors

2.25 Article 38.1 of the Directive requires Member States to ensure that statutory auditors or audit firms are only dismissed where there are proper grounds. Divergence of opinions on accounting treatments or audit procedures shall not be proper grounds. This provision relates to the need to provide protection for the independence of the auditor, for example in situations where they might come under undue pressure from the directors.

2.26 This requirement is not met for building societies or friendly societies. BERR are implementing this requirement in relation to companies by amending the unfair prejudice provisions of the Companies Act 2006 (s.994). BERR's consultation document and response give further details of this. However, there are no equivalent unfair

prejudice provisions in the Building Societies Act 1986 or the Friendly Societies Act 1992.

2.27 The Government has considered various options to deal with the specific issue here including the following: (a) do nothing, (b) the creation an equivalent remedy to unfair prejudice and (c) introducing a new right to apply to the High Courts. The Government considers that the “do nothing” option does not offer a pragmatic solution. It would also mean that we would not be implementing the Directive fully. Also that creating an equivalent remedy to unfair prejudice would go beyond the scope of the Directive for mutual societies and so would be gold-plating.

2.28 The Government therefore proposes to implement this requirement in relation to building societies and friendly societies by introducing a new right to apply to the High Court in cases where a society’s auditor is alleged to have been removed from office on unfair grounds. The right to apply to the High Court will be available to any member of the society who was also a member at the time of the removal, and to the Financial Services Authority. Where an application is successful, the High Court may give such relief as it thinks fit, including declaring that a resolution of the society removing an auditor is void, and requiring the directors of the society to re-appoint the auditor until the next general meeting of the society.

2.29 This will be implemented by amending Schedule 11 to the Building Societies Act 1986 and Schedule 14 to the Friendly Societies Act 1992 (see Part 2 of the Schedule to the Building Societies Act Order and the Friendly Societies Act Order).

2.30 There are a number of differences to the implementation proposed for companies. The right to apply to the High Court is available to the Financial Services Authority as well as to society members. This is considered appropriate in view of the FSA’s general regulatory role for building societies and friendly societies. Also, building society and friendly society members are mainly individuals, who are unlikely to bring legal action in relation to the dismissal of auditors. This contrasts to company members, who are often institutional shareholders with an interest in audit and corporate governance matters.

2.31 The right to apply to the court is only available to those members of the society who were members at the time of the dismissal. This is considered appropriate to limit access to the new right. It would be easy to become a member of a building society or a friendly society after a dismissal had taken place.

2.32 The implementing provisions for building societies and friendly societies also set out some courses of action, which the court may take if it finds that an auditor has been removed on improper grounds. This is intended to indicate possible or likely courses of action for the court, for the benefit of all parties, without in any way limiting the court’s power under the new provisions.

2.33 The new provisions only apply to friendly societies, which appoint statutory auditors, i.e. those that are within the scope of the Insurance Directive.

10. Do you have any comments on the Government's proposed implementation of Article 38.1 in relation to building societies and friendly societies?

11. Do you consider that the right to apply to the High Court, the availability of this right, and the powers given to the court, are appropriate?

12. Do you have any views on the costs and benefits of the proposal for (a) society members; (b) societies; (c) others?

2.34 Article 38.2 of the Directive requires Member States to ensure that the audited entity and the auditor inform the appropriate audit authority where an auditor is dismissed, and give reasons for the dismissal. For companies this requirement is met in sections 522 and 523 of the Companies Act 2006. It is not at present met for building societies or friendly societies.

2.35 The Government proposes to implement this requirement by imposing similar requirements in relation to building societies and friendly societies to those imposed in relation to companies by sections 522 and 523. The new provisions will require the auditor to notify the appropriate audit authority if he ceases for any reason to hold office, and the society to notify the appropriate audit authority if its auditor ceases to hold office before the end of his term. In both cases the notice must include reasons.

2.36 The "appropriate audit authority" is the Secretary of State or any person to whom the Secretary of State has delegated the function of receiving the equivalent notice under s.522 or 523 of the Companies Act 2006, such as the Professional Oversight Board.

2.37 Failure to comply with the new requirements is an offence, and the penalty is an (unlimited) fine on indictment, or a fine not exceeding the statutory maximum on summary conviction. The offence, and the penalty, is the same as those, which relate to companies in sections 522 and 523 of the 2006 Act.

2.38 There are some minor differences between the proposed provisions for building societies and friendly societies and those for companies. Some of the company law provisions distinguish between a "major audit" and other audits; there is no such distinction for building societies or friendly societies. There are also some differences in the timing of the notice, which reflect differences between company law and building society and friendly society law.

2.39 The new requirements will apply to all friendly societies, which are within the scope of the audit provisions of the 1992 Act. The provisions of this Article are all covered by the BERR/FSA implementation.

13. Do you agree that it is appropriate for the provisions on notifying the appropriate audit authority of an auditor's dismissal or resignation to mirror the implementing provisions for companies?

14. Do you have any comments on the costs and benefits of the proposals?

15. Do you have any other comments on the proposals?

Auditor remuneration for non-audit work

2.40 Article 49.1(a) of the Directive requires audited entities to specify separately in the notes to the annual accounts the fees paid to the statutory auditor for:

- the statutory audit;
- other assurance services;
- tax advice;
- all other services.

This requirement must be applied to building societies and to those friendly societies, which are within the scope of the Insurance Directive.

2.41 For companies, BERR is implementing Article 49 in the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2007. A draft of these regulations was published on the BERR website for comment in July. Following consideration of responses to the draft regulations, BERR issued a revised draft of the regulations for comment on 17 December 2007. It is available at <http://www.berr.gov.uk/bbf/co-act-2006/draft/page40411.html>. The closing date for comments will be 31 January 2008.

2.42 The existing provisions for building societies and friendly societies on disclosure of auditor remuneration for non-audit work do not meet the requirements of the Directive.

2.43 The Government proposes to implement Article 49.1(a) in relation to building societies and friendly societies by amending the relevant provisions of the Building Societies Act 1986 and the Friendly Societies Act 1992 to bring them into line with company law.

2.44 The Building Societies Act Order amends the provisions in Schedule 10A to the 1986 Act concerning the disclosure of auditors' remuneration and the definition of "associates" of a society's auditors. It also amends section 72J of the 1986 Act to require auditors to supply such information as is necessary to enable the information required by Schedule 10A to be given. Failure to supply the information is an offence, with a maximum level 3 fine (£1,000) on summary conviction.

2.45 The Friendly Societies Act Order makes similar amendments to the Friendly Societies Act 1992 (section 69J and Schedule 13D). The changes apply to all friendly societies covered by the audit provisions of the 1992 Act. The amendments are consistent with the equivalent company law provisions.

16. Do you have any comments on the Government's proposed implementation of Article 49 in relation to building societies and friendly societies?

Directive 2006/46/EC

2.46 The overall objective behind this Directive is to further enhance confidence in the financial statements and annual reports published by European companies. The HMT implementation strategy for this Directive will seek to achieve this objective by making financial arrangements more transparent and requiring the affected entities to give information relevant to good governance whilst seeking to avoid placing unnecessary burdens on business.

2.47 The specific measures in this Directive relevant to this consultation are in relation to the option to extend the application of “Fair Value” accounting to building societies and friendly societies, disclosure requirements in respect of off-balance sheet arrangements, and related party transactions .

Financial thresholds for defining SME’s

2.48 Article 1.1, 1.2 and 1.3 of the Directive gives Member States the option to increase the financial thresholds used to define SME’s for the purposes of the 4th and 7th Directives by 20% (Euros) for all eligible companies. These provisions do not affect the Bank Accounts Directive or the Insurance Accounts Directive, so they are not relevant to building societies or friendly societies.

Fair Value Accounting

2.49 Article 1.5 of the Directive provides Member States with the option to permit or require Fair Value accounting for the valuation and disclosure of a larger category of financial instruments than is permitted at present, together with associated disclosure requirements. The background to this change is set out in detail in BERR’s consultation document on implementation of this Directive (see paragraphs 3.14 - 3.22).

2.50 The BERR consultation proposes to permit, but not require, all companies preparing accounts under the Companies Act using UK Financial Reporting Standards to use fair value in accordance with IAS 39 in both their individual and consolidated accounts. This will be implemented in the Regulations restating the accounting schedules of the Companies Act 1985. See the BERR consultation response, paragraph 14, for details.

2.51 The Government proposes to implement an identical change for building societies and friendly societies. This will allow societies preparing accounts in accordance with UK Generally Accepted Accounting Practice (GAAP) under the Building Societies Act or Friendly Societies Act (rather than in accordance with IAS) to follow accounting best practice, make their balance sheets more transparent at the balance sheet date, and create greater confidence for investors and members.

2.52 The changes will be implemented by amending the Building Societies (Accounts and Related Provisions) Regulations 1998 and the Friendly Societies (Accounts and Related Provisions) Regulations 1994. The amendments will bring the Regulations into line with the equivalent company law provisions.

17. Do you agree that the option to use fair value accounting for a larger category of financial instruments should be extended to societies, which prepare their accounts in accordance with UK GAAP?

18. Do you have any comments on the proposed changes?

Disclosure requirements for off-balance sheet arrangements

2.53 Article 1.6 of the Directive amends the 4th Directive to require companies to disclose “off-balance sheet arrangements” in the notes to their annual accounts. An off balance sheet transaction usually means a corporate transaction, asset, debt or financing activity structured so that they do not appear on the company’s balance sheet even though in some instances they may materially affect the company’s available credit, cash position, liabilities etc.

2.54 The requirements of the Directive are also incorporated into the Insurance Accounts Directive (1991/674) and the Banking Accounts Directive (1986/635) so this

requirement will apply to friendly society insurers within the scope of the insurance Directives and to building societies.

2.55 BERR propose to implement this requirement by amending the Companies Act 2006 to require all companies, whether using EU adopted International Financial Reporting Standards (IFRS) or preparing Companies Act accounts, to disclose off-balance sheet arrangements. The draft amending regulations are available on the BERR website.

2.56 The Government proposes to implement this in a similar way for building societies and friendly societies. The requirement will apply to all building societies and friendly societies within the scope of the Directive, whether they prepare their accounts in accordance with the Building Societies or Friendly Societies Acts or in accordance with IAS. Amendments to the Building Societies Act 1986 and the Friendly Societies Act 1992 will be required.

2.57 The draft Building Societies Act Order inserts a new section 72L into the Building Societies Act 1986, which requires certain information relating to off-balance sheet arrangements to be given in the notes to the annual accounts. The draft Friendly Societies Act Order makes a similar amendment to the Friendly Societies Act 1992, inserting a new section 69L. The amendments are based on the equivalent company law provisions.

19. Do you have any comments on the Government's proposed implementation of the requirements relating to off-balance sheet transactions?

Related party transactions

2.58 The Directive proposes changes to disclosure requirements for related party transactions for companies and other entities preparing accounts under national legislation implementing the accounting Directives. The changes require disclosure in the notes to the accounts of transactions entered into by the company with related parties if they are material and have not been concluded under normal market conditions. .

2.59 BERR intend to implement this requirement in relation to companies in the regulations restating the Companies Act 1985. The draft regulations are published on the BERR website (see the BERR consultation response for references).

2.60 The Government proposes to implement this in the same way for building societies and friendly societies that prepare their accounts under the Building Societies or Friendly Societies Acts rather than in accordance with international accounting standards.

2.61 The changes will be made by amending the Building Societies (Accounts and Related Provisions) Regulations 1998 and the Friendly Societies (Accounts and Related Provisions) 1994. Details are in the draft amending regulations published in Chapter 3. They are based on the equivalent company law provisions.

20. Do you have any comments on the Government's proposed implementation of the requirements on related party transactions?

Annual corporate governance statement

2.62 Article 1.7 of the Directive applies to companies and other bodies incorporated in an EU Member State whose securities are traded on a regulated market in the EU. It imposes a requirement to produce an annual corporate governance statement in the annual ('directors') report or as a separate report, and specifies what the statement must contain.

2.63 Following BERR's consultation on the Directive, the Government concluded, with the agreement of the FSA, that this requirement should be implemented via the FSA Rules made under Part 6 of the Financial Services and Markets Act 2000 (as amended by the Companies Act 2006). See the BERR consultation response (paragraph 21) for details.

2.64 The only building societies and friendly societies affected by this provision will be those whose securities are traded on a regulated market. They will be within the scope of the rules being made by the FSA. So no further implementation is required.

Collective responsibility of board members

2.65 Articles 1.8, 1.9, 1.10 and 2.3 of the Directive require board members to be collectively responsible for the preparation and publication of the annual accounts and reports.

2.66 These requirements are already covered for building societies and friendly societies, as they are for companies. Sections 72A and 72E of the Building Societies Act 1986 set out the directors' collective responsibility for preparing individual and group accounts. Section 75 covers their responsibility for producing an annual report. Section 80 covers signature of the balance sheet (with the report attached). The criminal penalties for failure to comply with these requirements are set out in sections 75 and 80. The equivalent provisions in the Friendly Societies Act 1992 are sections 69A and 69E (duty to prepare accounts), 71 (duty of committee of management to produce annual report) and 76 (duty to sign accounts), and the penalties are set out in sections 71 and 76.

21. Do you agree that no further action needs to be taken in respect of the provisions on the corporate governance statement and the collective responsibility of board members?

Other changes to building society and friendly society legislation

2.67 The draft Statutory Instruments make a number of other minor amendments to the Building Societies Act 1986, the Friendly Societies Act 1992, and the Friendly Societies (Accounts and Related Provisions) Regulations 1994. These amendments:

- update references to "EEA State" in the Building Societies Act 1986 and Friendly Societies Act 1992;
- revoke certain provisions of the Friendly Societies (Accounts and Related Provisions) Regulations which since 2005 have been contained in the Friendly Societies Act 1992.

Further details are given in the explanatory notes to the draft Statutory Instruments.

Draft laid before Parliament under section 104(5) of the Building Societies Act 1986 and section 2(2) of the European Communities Act 1972, for approval by resolution of each House of Parliament.

D R A F T S T A T U T O R Y I N S T R U M E N T S

2008 No. xxxx

BUILDING SOCIETIES

**The Building Societies Act 1986 (Accounts, Audit and EEA State
Amendments) Order 2008**

<i>Made</i> - - - -	***
<i>Coming into force</i> - -	<i>6th April 2008</i>

A draft of this Order has been laid before Parliament in accordance with section 104(5) of the Building Societies Act 1986⁽¹⁾ and section 2(2) of the European Communities Act 1972⁽²⁾ and approved by both Houses of Parliament.

The Treasury is a department designated⁽³⁾ in relation to measures regulating the business of building societies and in relation to auditors and the audit of accounts.

The Treasury, in exercise of the powers conferred by section 104(1), (3) and (4) of the Building Societies Act 1986 and by section 2(2) of the European Communities Act 1972, make the following Order.

PART 1
INTRODUCTORY

Citation, commencement and application

1.—(1) This Order may be cited as the Building Societies Act 1986 (Accounts, Audit and EEA State Amendments) Order 2008.

(2) This Order comes into force on 6th April 2008.

(3) Articles 3 to 6 and Schedule 1 apply only in relation to—

- (a) financial years beginning on or after 6th April 2008, and
- (b) auditors appointed for those financial years.

(1) 1986 c.53.

(2) 1972 c.68.

(3) S.I. 2001/3495 and S.I. 2007/1679.

Interpretation

2. In this Order “the 1986 Act” means the Building Societies Act 1986.

PART 2 ACCOUNTS AND AUDIT

Disclosures relating to off-balance-sheet arrangements

3. After section 72K of the 1986 Act (disclosures about related undertakings required in notes to accounts), insert—

“Disclosures relating to off-balance-sheet arrangements required in notes to accounts

72L.—(1) If in any financial year—

- (a) a building society is or has been party to arrangements that are not reflected in its balance sheet, and
 - (b) at the balance sheet date the risks or benefits arising from those arrangements are material,
- the information required by this section must be given in notes to the society’s annual accounts.

(2) The information required is—

- (a) the nature and business purpose of the arrangements, and
- (b) the financial impact of the arrangements on the society.

(3) The information need only be given to the extent necessary for enabling the financial position of the society to be assessed.

(4) Where a building society is required to prepare consolidated group accounts, this section applies in relation to those accounts as if the undertakings included in the consolidation were a single building society.”.

Disclosure of auditor remuneration

- 4.—(1) After section 72L of the 1986 Act (inserted by Article 3), insert—

“Disclosure of auditor remuneration required in notes to accounts

72M.—(1) The information specified in Schedule 10C must be given in notes to a building society’s annual accounts.

(2) The Treasury may, by order, modify the provisions of Schedule 10C.

(3) An order under this section may—

- (a) make consequential amendments of or repeals in other provisions of this Act;
- (b) make such transitional or saving provisions as appear to the Treasury to be necessary or expedient;
- (c) make different provision for different cases.

(4) The power to make an order under this section is exercisable by statutory instrument but no such order shall be made unless a draft of it has been laid before and approved by a resolution of each House of Parliament.

(5) In this section “modify” includes amend, add to or repeal.”.

- (2) In Schedule 10A to the 1986 Act (disclosures about directors, other officers and employees in notes to accounts), omit paragraphs 11 and 12.

- (3) Schedule 1, which inserts Schedule 10C into the 1986 Act, has effect.

Signature of auditor's report

5. For section 78A of the 1986 Act (signature of auditors' report), substitute—

“Signature of auditor's report

78A.—(1) The auditor's report must state the name of the auditor and be signed and dated.

(2) Where the auditor is an individual, the report must be signed by him.

(3) Where the auditor is a firm, the report must be signed by the senior statutory auditor in his own name, for and on behalf of the auditor.

Senior statutory auditor

78B.—(1) The senior statutory auditor means the individual identified by the firm as senior statutory auditor in relation to the audit in accordance with the standards or guidance mentioned in section 504(1) of the Companies Act 2006.

(2) The person identified as senior statutory auditor must be eligible for appointment as auditor of the building society in question (see Chapter 2 of Part 42 of the Companies Act 2006).

(2) The senior statutory auditor is not, by reason of being named or identified as senior statutory auditor or by reason of his having signed the auditor's report, subject to any civil liability to which he would not otherwise be subject.

Names to be stated in copies of auditor's report filed or published

78C.—(1) The copy of the auditor's report sent to the Authority under section 81, and every copy of the auditor's report that is published by or on behalf of the society, must—

- (a) state the name of the auditor and (where the auditor is a firm) the name of the person who signed it as senior statutory auditor, or
- (b) if the conditions in section 78D (circumstances in which names may be omitted) are met, state that a resolution has been passed and notified to the Authority in accordance with that section.

(2) For the purposes of this section a building society is regarded as publishing the report 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.

(3) If a copy of the auditor's report is sent to the Authority or published without the statement required by this section, an offence is committed by—

- (a) the society, and
- (b) every officer of the society who is in default.

(4) A person guilty of an offence under this section is liable on summary conviction to a fine not exceeding level 3 on the standard scale.

Circumstances in which names may be omitted

78D.—(1) The auditor's name and, where the auditor is a firm, the name of the person who signed the report as senior statutory auditor, may be omitted from—

- (a) the copy of the report sent to the Authority under section 81, and
- (b) published copies of the report,

if the following conditions are met.

(2) The conditions are that the building society—

- (a) considering on reasonable grounds that statement of the name would create or be likely to create a serious risk that the auditor or the senior statutory auditor, or any other person, would be subject to violence or intimidation, has resolved by an ordinary resolution that the name should not be stated, and
- (b) has given notice of the resolution to the Authority, stating—

- (i) the name of the society,
- (ii) the financial year of the society to which the report relates, and
- (iii) the name of the auditor and (where the auditor is a firm) the name of the person who signed the report as senior statutory auditor.”.

Removal and resignation of auditors

6.—(1) Schedule 11 to the 1986 Act (auditors: appointment, tenure, qualifications) is amended as follows.

(2) After paragraph 6, insert—

“Removal of auditor on improper grounds

6A.—(1) Where an auditor of a building society is removed from office an application may be made to the High Court under this paragraph.

(2) The persons who may make such an application are—

- (a) any member of the society who was also a member at the time of the removal;
- (b) the Authority.

(3) If the court is satisfied that the removal was—

- (a) on grounds of divergence of opinion on accounting treatments or audit procedures, or
- (b) on any other improper grounds,

it may make such order as it thinks fit for giving relief in respect of the removal.

(4) The court may, in particular—

- (a) declare that any resolution of the society removing an auditor, or appointing a new auditor in his place, is void;
- (b) require the directors of the society to re-appoint the auditor until the next general meeting of the society;
- (c) give directions as to the conduct of the society’s affairs in the future.”.

(3) After paragraph 8 insert—

“Duty of auditor to notify appropriate audit authority

8A.—(1) Where an auditor of a building society ceases for any reason to hold office, he must notify the appropriate audit authority.

(2) The notice must—

- (a) inform the appropriate audit authority that he has ceased to hold office, and
- (b) if the auditor resigns, be accompanied by a copy of the auditor’s notice of resignation.

(3) The notice required by this paragraph must also be accompanied by a statement of the reasons for his ceasing to hold office unless—

- (a) the auditor resigns, and
- (b) the notice of resignation contains a statement under paragraph 7(2)(b).

(4) The auditor must comply with this paragraph—

- (a) if the auditor resigns, at the same time as he deposits his notice of resignation at the principal office of the building society;
- (b) in any other case, not later than the end of the period of fourteen days beginning with the date on which he ceases to hold office.

(5) A person ceasing to hold office as auditor who fails to comply with this paragraph commits an offence.

(6) If that person is a firm an offence is committed by—

- (a) the firm, and
- (b) every officer of the firm who is in default.

- (7) A person guilty of an offence under this paragraph is liable—
- (a) on conviction on indictment, to a fine;
 - (b) on summary conviction, to a fine not exceeding the statutory maximum.

Duty of building society to notify appropriate audit authority

8B.—(1) Where an auditor ceases to hold office before the end of his term of office, the building society must notify the appropriate audit authority.

- (2) The notice must—
- (a) inform the appropriate audit authority that the auditor has ceased to hold office, and
 - (b) be accompanied by—
 - (i) a statement by the society of the reasons for his ceasing to hold office, or
 - (ii) if the auditor resigns, and his notice of resignation contains a statement under paragraph 7(2)(b), a copy of that statement.
- (3) The society must give notice under this paragraph—
- (a) if the auditor resigns, not later than the end of the period of fourteen days beginning with the date on which the auditor’s notice of resignation is deposited at the society’s principal office;
 - (b) in any other case, not later than the end of the period of fourteen days beginning with the date on which the auditor ceases to hold office.
- (4) If a building society fails to comply with this paragraph, an offence is committed by—
- (a) the society, and
 - (b) every officer of the society who is in default.
- (5) A person guilty of an offence under this paragraph is liable—
- (a) on conviction on indictment, to a fine, and
 - (b) on summary conviction, to a fine not exceeding the statutory maximum.

Meaning of “appropriate audit authority”

8C. In paragraphs 8A and 8B above “appropriate audit authority” means—

- (a) the Secretary of State, or
- (b) if the Secretary of State has delegated functions under section 1252 of the Companies Act 2006 to a body whose functions include receiving the equivalent notice under section 522 or 523 of that Act, that body.”.

Consequential amendments

7. Schedule 2, which contains consequential amendments of the 1986 Act, has effect.

PART 3
EEA STATES

Amendment of definition of “EEA State”

8. In section 97 of the 1986 Act (transfer of business to commercial company), in subsection (13), for the words from “means a Contracting Party” to the end, substitute “has the meaning given by Schedule 1 to the Interpretation Act 1978”.

name

xx xx 2008

Two of the Lords Commissioners of Her Majesty's Treasury

name

SCHEDULE 1

Article 4(3)

Disclosure of auditor remuneration

After Schedule 10B to the 1986 Act insert—

“SCHEDULE 10C

Section 72M

Disclosure of auditor remuneration etc required in notes to accounts

Disclosure required

1.—(1) The following must be shown—

- (a) the amount of any remuneration receivable by the society's auditor for the auditing of the annual accounts, and
- (b) the amount of any remuneration receivable in respect of the financial year by—
 - (i) the society's auditor, or
 - (ii) any person who was, at any time during that financial year, an associate of the society's auditor,

for the supply of other services to the society or any associate of the society.

(2) Where the remuneration includes benefits in kind, the nature and estimated money-value of those benefits must also be shown.

(3) Separate disclosure is required in respect of the auditing of the accounts in question and of each type of service specified in paragraph 2, but not in respect of each service falling within a type of service.

(4) Separate disclosure is required in respect of services supplied to the society and its subsidiaries on the one hand and to associated pension schemes on the other.

(5) Where more than one person has been appointed as a society's auditor in respect of the financial year, separate disclosure is required in respect of the remuneration of each such person and his associates.

(6) Where a building society is required to prepare consolidated group accounts—

- (a) those accounts must comply with sub-paragraph (1)(b) as if the undertakings included in the consolidation were a single building society, and
- (b) notes to the society's individual accounts do not have to disclose the information required by that provision if the notes state that the group accounts are so required.

Types of service

2. The types of service in respect of which disclosure is required are—

- (a) the auditing of accounts of associates of the society pursuant to legislation (including that of countries and territories outside the United Kingdom);
- (b) other services supplied pursuant to such legislation;
- (c) other services relating to taxation;
- (d) services relating to information technology;
- (e) internal audit services;
- (f) valuation and actuarial services;
- (g) services relating to litigation;

- (h) services relating to recruitment and remuneration;
- (i) services relating to corporate finance transactions entered into or proposed to be entered into on behalf of the society or any of its associates;
- (j) all other services.

Duty of auditor to supply information

3. The auditor of a building society must supply the directors of the society with such information as is necessary to enable the disclosure required by paragraph 1 to be made.

Meaning of “associate” of auditor

4.—(1) This paragraph defines what is meant in paragraph 1 by an “associate” of a building society’s auditor.

(2) The following are associates of a society’s auditor—

- (a) any person controlled by the society’s auditor or by any associate of the society’s auditor (whether alone or through two or more persons acting together to secure or exercise control), but only if that control does not arise solely by virtue of the society’s auditor or any associate of the society’s auditor acting—
 - (i) as an insolvency practitioner in relation to any person,
 - (ii) in the capacity of a receiver, or a receiver or manager, of the property of a society or other body corporate, or
 - (iii) as a judicial factor on the estate of any person;
- (b) any person who, or group of persons acting together which, has control of the society’s auditor;
- (c) any person using a trading name which is the same as or similar to a trading name used by the society’s auditor, but only if the society’s auditor uses that trading name with the intention of creating the impression of a connection between the auditor and that other person;
- (d) any person who is party to an arrangement with the society’s auditor, with or without any other person, under which costs, profits, quality control, business strategy or significant professional resources are shared.

(2) Where the society’s auditor is a partnership, the following are also associates of the auditor—

- (a) any other partnership which has a partner in common with the society’s auditor;
- (b) any partner in the society’s auditor;
- (c) any body corporate which is in the same group as a body corporate which is a partner in the society’s auditor or in a partnership which has a partner in common with the society’s auditor;
- (d) any body corporate of which a partner in the society’s auditor is a director.

(3) Where a society’s auditor is a body corporate (other than one which is also a partnership as defined in subsection (4)(d)), the following are also associates of the auditor—

- (a) any other body corporate which has a director in common with the society’s auditor;
- (b) any director of the society’s auditor;
- (c) any body corporate which is in the same group as a body corporate which is a director of, or has a director in common with, the society’s auditor;
- (d) any partnership in which a director of the society’s auditor is a partner;
- (e) any body corporate which is in the same group as the society’s auditor;
- (f) any partnership in which any such body corporate which is in the same group as the society’s auditor is a partner.

(4) For the purposes of this section—

- (a) “acting as an insolvency practitioner” shall be construed in accordance with section 388 of the Insolvency Act 1986;

- (b) “director” includes any person occupying the position of director, by whatever name called;
- (c) “partner” includes a member of a limited liability partnership;
- (d) “partnership” includes a limited liability partnership and a partnership constituted under the law of a country or a territory outside the United Kingdom;
- (e) a reference to “a receiver, or a receiver or manager, of the property of a society or other body corporate” includes a receiver, or (as the case may be) a receiver or manager, of part only of that property;
- (f) a person able, directly or indirectly to control or materially to influence the operating and financial policy of another person shall be treated as having control of that other person; and
- (g) a body corporate is in the same group as another body corporate if one is a subsidiary of the other.

Interpretation

5. In this Schedule—

“associate of the society” means—

- (a) any subsidiary of the society, other than a subsidiary in respect of which severe long-term restrictions substantially hinder the exercise of rights of the society over the assets or management of that subsidiary, or
- (b) any associated pension scheme;

“associated pension scheme”, in relation to a building society, means a scheme for the provision of benefits for or in respect of directors or employees (or former directors or employees) of the society or any subsidiary of the society where—

- (a) the benefits consist of or include any pension, lump sum, gratuity or other like benefit given or to be given on retirement or on death or in anticipation of retirement or, in connection with past service, after retirement or death, and
- (b) either—
 - (i) a majority of the trustees are appointed by, or by a person acting on behalf of the society or a subsidiary of the society, or
 - (ii) the society, or a subsidiary of the society, exercises a dominant influence over the appointment of the auditor (if any) of the scheme;

“remuneration” includes payments in respect of expenses and benefits in kind;

“subsidiary” means a subsidiary undertaking that is a body corporate.”.

SCHEDULE 2

Article 7

Consequential amendments of the 1986 Act

1. The 1986 Act is amended as follows.
2. In section 74 (duty of directors to prepare annual business statement), in subsection (6), for “auditors” substitute “auditor”.
3. In section 76 (summary financial statement for members and depositors)—
 - (a) in subsection (5), for “auditors’ opinion” substitute “auditor’s opinion”;
 - (b) in subsection (8A)(b), for “auditors’ report” substitute “auditor’s report” in both places where it occurs;
 - (c) in subsection (9), for “auditors’ report” substitute “auditor’s report” in both places where it occurs.
4. In section 78 (auditors’ report)—
 - (a) in subsection (1)—

- (i) for “auditors” substitute “auditor”;
- (ii) for “their” substitute “his”;
- (b) in subsection (2), for “auditors’ report” substitute “auditor’s report”;
- (c) in subsection (3), for “auditors shall, in their” substitute “auditor shall, in his”;
- (d) in subsection (3A), for “auditors’ report” substitute “auditor’s report”;
- (e) in subsection (3B), for “auditors’ opinion” substitute “auditor’s opinion”;
- (f) in subsection (4A)—
 - (i) in the opening words, for “auditors’ report” substitute “auditor’s report”;
 - (ii) in paragraph (b), for “auditors wish” substitute “auditor wishes”;
- (g) in subsection (6)—
 - (i) for “auditors’ report” substitute “auditor’s report” in both places where it occurs;
 - (ii) for “their opinion” substitute “his opinion”;
- (h) in subsection (7)—
 - (i) for “auditors’ report” substitute “auditor’s report”;
 - (ii) for “they have” substitute “he has”;
- (iii) for “auditors” substitute “auditor”;
- (i) in subsection (8), for “auditors’ report” substitute “auditor’s report”;
- (j) in subsection (9), for “auditors” substitute “auditor”;
- (k) in subsection (10)—
 - (i) for “auditors’ report” substitute “auditor’s report”;
 - (ii) for “their opinion” substitute “his opinion” in both places where it occurs;
 - (iii) for “they shall include in their” substitute “he shall include in his”;
 - (iv) for “they are” substitute “he is”;
- (l) in the heading, for “Auditors’ report” substitute “Auditor’s report”.

5. In section 79 (auditors’ duties and powers)—

- (a) in subsection (1)—
 - (i) for “auditors” substitute “auditor”;
 - (ii) for “their” substitute “his”;
 - (iii) for “them” substitute “him”;
- (b) in subsection (2)—
 - (i) for “auditors are” substitute “auditor is”;
 - (ii) for “they” substitute “he”;
- (c) in subsection (4)(a)—
 - (i) for “its auditors” substitute “its auditor”;
 - (ii) for “the society’s auditors” substitute “the society’s auditor”;
 - (iii) for “those auditors” substitute “that auditor”;
 - (iv) for “their duties as auditors” substitute “his duties as auditor”;
- (d) in subsection (6)—
 - (i) for “auditors fail” substitute “auditor fails”;
 - (ii) for “their” substitute “his”;
 - (iii) for “they” substitute “he”;
- (e) in subsection (7)—
 - (i) in the opening words, for “auditors” substitute “auditor”;

- (ii) in paragraph (b)—
 - (aa) for “they attend” substitute “he attends”;
 - (bb) for “them as auditors” substitute “him as auditor”;
- (f) in subsection (9)—
 - (i) in the opening words, for “auditors” substitute “auditor”;
 - (ii) in paragraph (a), for “auditors require, or are entitled to require, as auditors” substitute “auditor requires, or is entitled to require, as auditor”;
 - (g) in the heading, for “Auditors’ duties and powers” substitute “Auditor’s duties and powers”.

6. In section 80 (signing of balance sheet: documents to be annexed), in subsection (6)(d), for “auditors’ report” substitute “auditor’s report”.

7. In section 81A (requirements in connection with publication of accounts)—

- (a) in subsection (1), for “auditors’ report” substitute “auditor’s report”;
- (b) in subsection (3)—
 - (i) in paragraph (c), for “auditors have” substitute “auditor has”;
 - (ii) in paragraph (d)—
 - (aa) in the opening words, for “auditors’ report” substitute “auditor’s report”;
 - (bb) in sub-paragraph (i), for “auditors” substitute “auditor”;
 - (cc) in the closing words, for “auditors’ report” substitute “auditor’s report”.

8. In Schedule 11 (auditors: appointment, tenure, qualifications)—

- (a) in paragraph 1(1)—
 - (i) for “first auditors” substitute “first auditor”;
 - (ii) for “and auditors” substitute “and an auditor”;
- (b) in paragraph 3(1), for “auditors are” substitute “auditor is”.

EXPLANATORY NOTE

(This note is not part of the Order)

This Order amends the Building Societies Act 1986 (“the 1986 Act”) to give effect, in relation to building societies, to:

Parts of Directive 2006/43/EC of the European Parliament and of the Council on statutory audits of annual accounts (amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC) (O.J. L 157, 9.6.2006, p.87) (“the Audit Directive”), and

Parts of Directive 2006/46/EC of the European Parliament and of the Council 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 (O.J. L 224, 16.8.2006, p.7) (“the Accounts Directive”).

The Order also makes an amendment to the definition of “EEA State” in section 97 of the 1986 Act, which is necessary as a result of the recent accession of new member States to the European Community.

The parts of the Audit and Accounts Directives implemented by this Order are those which require amendments to the 1986 Act. The remainder of the Audit Directive will be implemented for building societies by and under the Companies Act 2006. The remainder of the Accounts Directive will be implemented for building societies by amendments to the Building Societies (Accounts and Related Provisions) Regulations 1998 (S.I. 1998/504).

Article 3 of the Order inserts a new section 72L into the 1986 Act, requiring building societies to give certain information relating to off-balance-sheet arrangements in the notes to their annual accounts. This implements part of Article 1.6 of the Accounts Directive.

Article 4, and Schedule 1, amend the requirements in the 1986 Act on the disclosure of auditor remuneration. This implements Article 49 of the Audit Directive.

Article 5 substitutes new sections 78A to 78D for section 78A of the 1986 Act. The new provisions relate to the signature of the auditor's report, the publication of auditors' names in the report and the circumstances in which they may be omitted. This implements Article 28.1 of the Audit Directive.

Article 6 amends Schedule 11 to the 1986 Act. New paragraph 6A gives members of the society, and the Financial Services Authority, the right to apply to the High Court (or in Scotland, the Court of Session) for an order giving relief in respect of the removal of an auditor on improper grounds. This implements Article 38.1 of the Audit Directive. New paragraphs 8A to 8C require the auditor and the building society to notify the appropriate audit authority where an auditor ceases to hold office. This implements Article 38.2 of the Audit Directive.

A transposition note showing how the main provisions of the Audit and Accounts Directives (as they apply to building societies) will be transposed into UK law is available from HM Treasury. Copies may be obtained from the Savings and Investment Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ and the note will be available on the Treasury website (www.hm-treasury.gov.uk).

A full regulatory impact assessment of the effect that this instrument will have on the costs of business is also available from HM Treasury at the above address, and is annexed to the Explanatory Memorandum which is available alongside the instrument on the OPSI website (www.opsi.gov.uk).

STATUTORY INSTRUMENTS

2008 No. xxxx

FRIENDLY SOCIETIES**The Friendly Societies Act 1992 (Accounts, Audit and EEA State
Amendments) Order 2008**

Made - - - - - ***
Laid before Parliament ***
Coming into force - - - - - 6th April 2008

The Treasury is a department designated⁽⁴⁾ in relation to measures regulating insurance business carried on by friendly societies and in relation to auditors and the audit of accounts.

The Treasury, in exercise of the powers conferred by section 102(1), (3) and (4) of the Friendly Societies Act 1992⁽⁵⁾ and section 2(2) of the European Communities Act 1972⁽⁶⁾, make the following Order:

PART 1
INTRODUCTORY**Citation, commencement and application**

9.—(1) This Order may be cited as the Friendly Societies Act 1992 (Accounts, Audit and EEA State Amendments) Order 2008.

(2) This Order comes into force on 6th April 2008.

(3) Articles 3 to 6 and Schedule 1 apply only in relation to—

- (a) financial years beginning on or after 6th April 2008, and
- (b) auditors appointed for those financial years.

Interpretation

10. In this Order “the 1992 Act” means the Friendly Societies Act 1992.

⁽⁴⁾ S.I. 2001/3495 and S.I. 2007/1679.

⁽⁵⁾ 1992 c.40.

⁽⁶⁾ 1972 c.68.

PART 2

ACCOUNTS AND AUDIT

Disclosures relating to off-balance-sheet arrangements

11. After section 69K of the 1992 Act, insert—

Disclosures relating to off-balance-sheet arrangements

“69L.—(1) If in any financial year—

(a) a friendly society or registered branch has been party to arrangements that are not reflected in its balance sheet, and

(b) at the balance sheet date the risks or benefits arising from those arrangements are material, the information required by this section must be given in notes to the society’s or branch’s annual accounts.

(2) The information required is—

(a) the nature and business purpose of the arrangements, and

(b) the financial impact of the arrangements on the society or branch.

(3) The information need only be given to the extent necessary for enabling the financial position of the society or branch to be assessed.

(4) Where a friendly society is required to prepare consolidated group accounts, this section applies in relation to those accounts as if the undertakings included in the consolidation were a single friendly society.”

Disclosure of auditor remuneration

12.—(1) After section 69L of the 1992 Act (inserted by Article 3), insert—

“Disclosure of auditor remuneration

69M.—(1) The information specified in Schedule 13F must be given in notes to a friendly society’s or a registered branch’s annual accounts.

(2) The Treasury may, by order, modify the provisions of Schedule 13F.

(3) An order under this section may—

(a) make consequential amendments or repeals of other provisions of this Act;

(b) make such transitional or saving provisions as appear to the Treasury to be necessary or expedient, or

(c) make different provision for different cases.”

(2) Schedule 1, which inserts Schedule 13F into the 1992 Act, has effect.

(3) In Schedule 13D to the 1992 Act (disclosures about members of the committee of management and employees) omit paragraph 12.

(4) In Schedule 14 to the 1992 Act (auditors: appointment, tenure, qualifications and remuneration)—

(a) in paragraph 16—

(i) omit sub-paragraphs (3) and (6);

(ii) in sub-paragraph (5), omit the words from “and in relation to any such benefit” to the end;

(b) omit paragraph 17.

Signature of auditor’s report

13.—(1) For section 74 of the 1992 Act (signature of auditors’ report), substitute—

“Signature of auditor’s report

74.—(1) The auditor’s report to the members of a friendly society or registered branch must state the name of the auditor and be signed and dated.

(2) Where the auditor is an individual, the report must be signed by him.

(3) Where the auditor is a firm, the report must be signed—

(a) in the case of a friendly society to which the Audit Directive applies, by the senior statutory auditor in his own name, for and on behalf of the firm;

(b) in any other case—

(i) in the name of the firm by a person authorised to sign on its behalf, or

(ii) if the firm has identified a senior statutory auditor in relation to the audit, by that person, in his own name, for and on behalf of the firm.

Senior statutory auditor

74A.—(1) The senior statutory auditor means the individual identified by the firm as senior statutory auditor in relation to the audit in accordance with the standards or guidance mentioned in section 504(1) of the Companies Act 2006.

(2) The person identified as senior statutory auditor must be eligible for appointment as auditor of the society in question in accordance with—

(a) in the case of a friendly society to which the Audit Directive applies, Chapter 42 of Part 42 of the Companies Act 2006;

(b) in any other case, Schedule 14 to this Act.

(3) The senior statutory auditor is not, by reason of being named or identified as senior statutory auditor or by reason of his having signed the auditor’s report, subject to any civil liability to which he would not otherwise be subject.

Names to be stated in copies of auditor’s report filed or published

74B.—(1) The copies of the auditor’s report sent to the Authority under section 78(1) or (2) below, and every copy of the auditor’s report that is published by or on behalf of the friendly society or registered branch, must—

(a) state the name of the auditor and (where the auditor is a firm and the report is signed by a senior statutory auditor) the name of the person who signed it as senior statutory auditor, or

(b) if the conditions in section 74C (circumstances in which names may be omitted) are met, state that a resolution has been passed and notified to the Authority in accordance with that section.

(2) For the purposes of this section a society or branch is regarded as publishing the report 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.

(3) If a copy of the auditor’s report is sent to the Authority or published without the statement required by this section, an offence is committed by—

(a) the society or branch, and

(b) every officer of the society or branch who is in default.

(4) A person guilty of an offence under this section is liable on summary conviction to a fine not exceeding level 3 on the standard scale.

Circumstances in which names may be omitted

74C.—(1) The auditor’s name, and (where applicable) the name of the person who signed the report as senior statutory auditor, may be omitted from—

(a) the copies of the report sent to the Authority under section 78(1) or (2) below, and

(b) published copies of the report,

if the following conditions are met.

- (2) The conditions are that the friendly society or registered branch—
 - (a) considering on reasonable grounds that statement of the name would create or be likely to create a serious risk that the auditor or senior statutory auditor, or any other person, would be subject to violence or intimidation, has resolved in general meeting that the name should not be stated, and
 - (b) has given notice of the resolution to the Authority, stating—
 - (i) the name of the society or branch,
 - (ii) the financial year of the society to which the report relates, and
 - (iii) the name of the auditor and (where applicable) the name of the person who signed the report as senior statutory auditor.”.

Removal or resignation of auditor

14.—(1) Schedule 14 to the 1992 Act (auditors: appointment, tenure, qualifications and remuneration) is amended as follows.

- (1) After paragraph 10, insert—

“Removal of auditor on improper grounds

10A.—(1) Where an auditor of a friendly society to which the Audit Directive applies is removed from office an application may be made to the High Court under this paragraph.

- (2) The persons who may make such an application are—
 - (a) any member of the society who was also a member at the time of the removal;
 - (b) the Authority.
- (3) If the court is satisfied that the removal was—
 - (a) on grounds of divergence of opinion on accounting treatments or audit procedures, or
 - (b) on any other improper grounds,

it may make such order as it thinks fit for giving relief in respect of the removal.

- (4) The court may, in particular—
 - (a) declare that any resolution of the society removing an auditor, or appointing a new auditor in his place, is void;
 - (b) require the directors of the society to re-appoint the auditor until the next general meeting of the society;
 - (c) give directions as to the conduct of the society’s affairs in the future.

(5) In the application of this paragraph to a friendly society whose registered office is in Scotland or Northern Ireland, references to the High Court shall be read as references to the Court of Session or, as the case may be, the High Court in Northern Ireland.”.

- (2) After paragraph 15 insert—

“Duty of auditor to notify appropriate audit authority

15A.—(1) Where an auditor of a friendly society or registered branch ceases for any reason to hold office, he must notify the appropriate audit authority.

- (2) The notice must—
 - (a) inform the appropriate audit authority that he has ceased to hold office, and
 - (b) be accompanied by a copy of the statement deposited by him at the registered office of the society or branch in accordance with paragraph 14.

(3) If the statement so deposited is to the effect that he considers that there are no circumstances in connection with his ceasing to hold office that need to be brought to the attention of the members or creditors of the society or branch, the notice must also be accompanied by a statement of the reasons for his ceasing to hold office.

(4) The auditor must comply with this paragraph at the same time as he deposits a statement at the registered office of the society or branch in accordance with paragraph 14.

(5) If a person ceasing to hold office as auditor fails to comply with this paragraph, he is guilty of an offence and liable—

- (a) on conviction on indictment, to a fine, and
- (b) on summary conviction, to a fine not exceeding the statutory maximum.

Duty of friendly society or registered branch to notify appropriate audit authority

15B.—(1) Where an auditor of a friendly society or registered branch ceases to hold office before the end of his term of office, the society or branch must notify the appropriate audit authority.

(2) The notice must—

- (a) inform the appropriate audit authority that the auditor has ceased to hold office, and
- (b) be accompanied by—
 - (i) a statement by the society or branch of the reasons for his ceasing to hold office, or
 - (ii) if the copy of the statement deposited by the auditor at the registered office of the society or branch in accordance with paragraph 14(1) contains a statement of circumstances connected with his ceasing to hold office which he considers should be brought to the attention of the members or creditors of the society or branch, a copy of that statement.

(3) The society or branch must give notice under this paragraph—

- (a) if the auditor resigns, not later than the end of the period of 14 days beginning with the date on which the auditor's notice of resignation is deposited at the society's or branch's registered office;
- (b) in any other case, not later than the end of the period of 14 days beginning with the date on which the auditor ceases to hold office.

(4) If a friendly society or registered branch fails to comply with this paragraph, it is guilty of an offence and liable—

- (a) on conviction on indictment, to a fine, and
- (b) on summary conviction, to a fine not exceeding the statutory maximum.

Meaning of "appropriate audit authority"

15C. In paragraphs 15A and 15B above "appropriate audit authority" means—

- (a) the Secretary of State, or
- (b) if the Secretary of State has delegated functions under section 1252 of the Companies Act 2006 to a body whose functions include receiving the equivalent notice under section 522 or 523 of that Act, that body."

Interpretation

15.—(1) Section 78A of the 1992 Act (interpretation of Part 6: accounts and audit) is amended as follows.

(2) In subsection (1) at the appropriate places insert—

““the Audit Directive” means Directive 2006/43/EC of the European Parliament and of the Council on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC (as to friendly societies to which the Directive applies, see subsection (3) below);”;

““firm” means any entity, whether or not a legal person, that is not an individual and includes a body corporate, a corporation sole, and a partnership or other unincorporated association;”;

““senior statutory auditor” has meaning given by section 74A(1) above;”.

(3) After subsection (2) insert—

“(3) References in this Part to a friendly society to which the Audit Directive applies are to a friendly society that is an insurance undertaking within the meaning given by Article 2.1 of Council Directive 1991/674/EEC on the annual accounts and consolidated accounts of insurance undertakings.”

(4) In paragraph 4(3) of Schedule 14, omit the definition of “firm”.

Parliamentary procedure for certain orders

16. In section 121(2) of the 1992 Act (orders and regulations), for “section 5, 69J or 69K” substitute “section 5”.

Consequential amendments

17. Schedule 2, which contains consequential amendments of the 1992 Act, has effect.

PART 3 EEA STATES

Amendment of definition of “EEA State”

18. In section 119(1) of the 1992 Act—

(a) omit the definition of “EEA Agreement”;

(b) for the definition of “EEA State”, substitute—

““EEA State” has the meaning given by Schedule 1 to the Interpretation Act 1978;”.

xx xx 2008

name
name

Two of the Lords Commissioners of Her Majesty’s Treasury

SCHEDULE 1

Article 4

Disclosure of auditor remuneration

After Schedule 13E to the 1992 Act (disclosures about related undertakings), insert—

“SCHEDULE 13F

Section 69M

Disclosure of auditor remuneration etc

Disclosure required

1.—(1) The following must be shown—

(a) the amount of any remuneration receivable by the society’s auditor for the auditing of the annual accounts, and

- (b) the amount of any remuneration receivable in respect of the financial year by—
 - (i) the society’s auditor, or
 - (ii) any person who was, at any time during that financial year, an associate of the society’s auditor,

for the supply of other services to the society or branch or any associate of the society or branch.

(2) Where the remuneration includes benefits in kind, the nature and estimated money-value of those benefits must also be shown.

(3) Separate disclosure is required in respect of the auditing of the accounts in question and of each type of service specified in paragraph 2, but not in respect of each service falling within a type of service.

(4) Separate disclosure is required in respect of services supplied to the society and its subsidiaries on the one hand and to associated pension schemes on the other.

(5) Where more than one person has been appointed as a society’s auditor in respect of the financial year, separate disclosure is required in respect of the remuneration of each such person and his associates.

(6) Where a friendly society is required to prepare consolidated group accounts—

- (a) those accounts must comply with sub-paragraph (1)(b) as if the undertakings included in the consolidation were a single friendly society, and
- (b) notes to the society’s individual accounts do not have to disclose the information required by that provision if the notes state that the group accounts are so required.

Types of service

2. The types of service in respect of which disclosure is required are—

- (a) the auditing of accounts of associates of the society pursuant to legislation (including that of countries and territories outside the United Kingdom);
- (b) other services supplied pursuant to such legislation;
- (c) other services relating to taxation;
- (d) services relating to information technology;
- (e) internal audit services;
- (f) valuation and actuarial services;
- (g) services relating to litigation;
- (h) services relating to recruitment and remuneration;
- (i) services relating to corporate finance transactions entered into or proposed to be entered into on behalf of the society or any of its associates;
- (j) all other services.

Duty of auditor to supply information

3. The auditor of a friendly society must supply the directors of the society with such information as is necessary to enable the disclosure required by paragraph 1(1)(b) to be made.

Meaning of “associate” of auditor

4.—(1) This paragraph defines what is meant in paragraph 1 by an “associate” of a friendly society’s auditor.

(2) The following are associates of a society’s auditor—

- (a) any person controlled by the society’s auditor or by any associate of the society’s auditor (whether alone or through two or more persons acting together to secure or exercise control), but only if that control does not arise solely by virtue of the society’s auditor or any associate of the society’s auditor acting—
 - (i) as an insolvency practitioner in relation to any person,

- (ii) in the capacity of a receiver, or a receiver or manager, of the property of a society or other body corporate, or
 - (iii) as a judicial factor on the estate of any person;
- (b) any person who, or group of persons acting together which, has control of the society's auditor;
 - (c) any person using a trading name which is the same as or similar to a trading name used by the society's auditor, but only if the society's auditor use that trading name with the intention of creating the impression of a connection between the auditor and that other person;
 - (d) any person who is party to an arrangement with the society's auditor, with or without any other person, under which costs, profits, quality control, business strategy or significant professional resources are shared.
- (2) Where the society's auditor is a partnership, the following are also associates of the auditor—
- (a) any other partnership which has a partner in common with the society's auditor;
 - (b) any partner in the society's auditor;
 - (c) any body corporate which is in the same group as a body corporate which is a partner in the society's auditor or in a partnership which has a partner in common with the society's auditor;
 - (d) any body corporate of which a partner in the society's auditor is a director.
- (3) Where a society's auditor is a body corporate (other than one which is also a partnership: see subparagraph (4)(d)), the following are also associates of the auditor—
- (a) any other body corporate which has a director in common with the society's auditor;
 - (b) any director of the society's auditor;
 - (c) any body corporate which is in the same group as a body corporate which is a director of, or has a director in common with, the society's auditor;
 - (d) any partnership in which a director of the society's auditor is a partner;
 - (e) any body corporate which is in the same group as the society's auditor;
 - (f) any partnership in which any such body corporate which is in the same group as the society's auditor is a partner.
- (4) For the purposes of this paragraph—
- (a) "acting as an insolvency practitioner" shall be construed in accordance with section 388 of the Insolvency Act 1986;
 - (b) "director" includes any person occupying the position of director, by whatever name called;
 - (c) "partner" includes a member of a limited liability partnership;
 - (d) "partnership" includes a limited liability partnership and a partnership constituted under the law of a country or a territory outside the United Kingdom;
 - (e) a reference to "a receiver, or a receiver or manager, of the property of a society or other body corporate" includes a receiver, or (as the case may be) a receiver or manager, of part only of that property;
 - (f) a person able, directly or indirectly to control or materially to influence the operating and financial policy of another person shall be treated as having control of that other person; and
 - (g) a body corporate is in the same group as another body corporate if one is a subsidiary of the other.

Interpretation

5. In this Schedule—

"associate of the society" means—

- (a) any subsidiary of the society, other than a subsidiary in respect of which severe long-term restrictions substantially hinder the exercise of rights of the society over the assets or management of that subsidiary; or
- (b) any associated pension scheme;

“associated pension scheme”, in relation to a friendly society, means a scheme for the provision of benefits for or in respect of committee members or employees (or former committee members or employees) of the society or any subsidiary of the society where—

- (a) the benefits consist of or include any pension, lump sum, gratuity or other like benefit given or to be given on retirement or on death or in anticipation of retirement or, in connection with past service, after retirement or death; and
- (b) either—
 - (i) a majority of the trustees are appointed by, or by a person acting on behalf of the society or a subsidiary of the society; or
 - (ii) the society, or a subsidiary of the society, exercises a dominant influence over the appointment of the auditor (if any) of the scheme;

“remuneration” includes payments in respect of expenses and benefits in kind;

“subsidiary” means a subsidiary undertaking that is a body corporate.

Application to registered branches

6. This Schedule applies to a registered branch as it applies to a friendly society.”.

SCHEDULE 2

Article 9

Consequential amendments of the 1992 Act

19. The 1992 Act is amended as follows.

20. In section 73 (auditors’ report)—

- (a) in subsection (1)—
 - (i) for “auditors” substitute “auditor”;
 - (ii) for “their” substitute “his”;
- (b) in subsection (2)—
 - (i) in the opening words—
 - (aa) for “auditors” substitute “auditor”;
 - (bb) for “their” substitute “his”;
 - (cc) for “them” substitute “him”;
 - (ii) in the closing words—
 - (aa) for “auditors are” substitute “auditor is”;
 - (bb) for “they” substitute “he”;
 - (cc) for “their” substitute “his”;
- (c) in subsection (3)—
 - (i) for “auditors fail” substitute “auditor fails”;
 - (ii) for “their” substitute “his”, in each place where it occurs;
 - (iii) for “they” substitute “he”;
- (d) in subsection (4A)—
 - (i) in the opening words, for “auditors shall, in their” substitute “auditor shall, in his”;
 - (ii) in paragraphs (a) and (b), for “their opinion” substitute “his opinion” in each place where it occurs;
- (e) in subsection (5A), for “auditors shall, in their” substitute “auditor shall, in his”;
- (f) in subsection (5B)—

- (i) for “auditors shall, in their” substitute “auditor shall, in his”;
- (ii) for “auditors’ opinion” substitute “auditor’s opinion”;
- (g) in subsection (5C), for “auditors shall, in their” substitute “auditor shall, in his”;
- (h) in subsection (5D)—
 - (i) for “auditors’ report” substitute “auditor’s report”;
 - (ii) in paragraph (b), for “auditors wish” substitute “auditor wishes”;
 - (i) in the heading, for “Auditors’ report” substitute “Auditor’s report”.

21. In section 75 (auditors’ rights to information and to attend meetings)—

- (a) in subsection (1)—
 - (i) in the opening words, for “auditors of a friendly society are” substitute “auditor of a friendly society is”;
 - (ii) in paragraph (b), for the words from “as they” to the end substitute “as he thinks necessary for the performance of his duties as auditor”;
 - (iii) in paragraph (d), for “them as auditors” substitute “him as auditor”;
 - (iv) in the closing words, for “auditors of a registered branch have” substitute “auditor of a registered branch has”;
- (b) in subsection (3)—
 - (i) in the opening words, for “auditors” substitute “auditor”;
 - (ii) in paragraph (a), for “auditors require, or are entitled to require, as auditors” substitute “auditor requires, or is entitled to require, as auditor”;
- (c) in subsection (4)—
 - (i) in the opening words, for “auditors” substitute “auditor”;
 - (ii) in paragraph (a), for “auditors require, or are entitled to require, as auditors”, substitute “auditor requires, or is entitled to require, as auditor”;
- (d) in subsection (6), in the closing words—
 - (i) for “the auditors” substitute “the auditor”, in both places where it occurs;
 - (ii) for “those auditors” substitute “that auditor”;
 - (iii) for “their duties as auditors” substitute “his duties as auditor”;
- (e) in subsection (8)—
 - (i) for “its auditors” substitute “its auditor”;
 - (ii) for “their duties of auditors” substitute “his duties as auditor”;
- (f) in the heading, for “Auditors’ rights” substitute “Auditor’s rights”.

22. In section 78 (laying and furnishing of accounts and reports), in subsections (1)(a), (2)(a), (3)(a) and (4)(a), for “auditors’ report” substitute “auditor’s report”, in each place where it occurs.

23. In Schedule 14 (Auditors: appointment, tenure, qualifications and remuneration)—

- (a) in paragraph 1(1)—
 - (i) for “first auditors” substitute “first auditor”;
 - (ii) for “and auditors” substitute “and an auditor”;
- (b) in paragraph 3(1), for “auditors are” substitute “auditor is”;
- (c) in paragraph 16, in sub-paragraphs (1) and (2), for “auditors” substitute “auditor”, in both places where it occurs.

EXPLANATORY NOTE

(This note is not part of the Order)

This Order amends the Friendly Societies Act 1992 (“the 1992 Act”) to give effect, in relation to friendly societies, to:

Parts of Directive 2006/43/EC of the European Parliament and of the Council on statutory audits of annual accounts (amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC) (O.J. L 157, 9.6.2006, p.87) (“the Audit Directive”), and

Parts of Directive 2006/46/EC of the European Parliament and of the Council 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 (O.J. L 224, 16.8.2006, p.7) (“the Accounts Directive”).

The Order also makes an amendment to the definition of “EEA State” in section 119 of the 1992 Act, which is necessary as a result of the recent accession of new member States to the European Community.

The parts of the Audit and Accounts Directives implemented by this Order are those which require amendments to the 1992 Act. The remainder of the Audit Directive will be implemented for friendly societies by and under the Companies Act 2006. The remainder of the Accounts Directive will be implemented for friendly societies by amendments to the Friendly Societies (Accounts and Related Provisions) Regulations 1994 (S.I. 1994/1983).

Article 3 of the Order inserts a new section 69L into the 1992 Act, requiring friendly societies to give certain information relating to off-balance-sheet arrangements in the notes to their annual accounts. This implements part of Article 1.6 of the Accounts Directive. Article 4, and Schedule 1, amend the requirements in the 1992 Act on the disclosure of auditors’ remuneration. This implements Article 49 of the Audit Directive.

Article 5 substitutes new sections 74 to 74C for section 74 of the 1992 Act. The new provisions relate to the signature of the auditor’s report, the publication of auditors’ names in the report and the circumstances in which they may be omitted. This implements Article 28.1 of the Audit Directive.

Article 6 amends Schedule 14 to the 1986 Act. New paragraph 10A gives members of the society, and the Financial Services Authority, the right to apply to the High Court (or in Scotland, the Court of Session) for an order giving relief in respect of the removal of an auditor on improper grounds. This implements Article 38.1 of the Audit Directive. New paragraphs 15A to 15C require the auditor and the friendly society to notify the appropriate audit authority where an auditor ceases to hold office. This implements Article 38.2 of the Audit Directive.

Article 8 corrects a defect in the 1992 Act made by the Friendly Societies Act 1992 (International Accounting Standards and Other Accounting Amendments) Order 2005 (S.I. 2005/2211). This relates to the parliamentary procedure applicable to the order-making powers in sections 69J and 69K. As the correction is made in an instrument making other amendments, this Order is not made available free of charge to those who bought the defective instrument.

A transposition note showing how the main provisions of the Audit and Accounts Directives (as they apply to friendly societies) will be transposed into UK law is available from HM Treasury. Copies may be obtained from the Savings and Investment Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ and the note will be available on the Treasury website (www.hm-treasury.gov.uk).

A full regulatory impact assessment of the effect that this instrument will have on the costs of business is also available from HM Treasury at the above address, and is annexed to the Explanatory Memorandum which is available alongside the instrument on the OPSI website (www.opsi.gov.uk).

 STATUTORY INSTRUMENTS

2008 No.

BUILDING SOCIETIES

The Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2008

<i>Made</i>	- - - -	***
<i>Laid before Parliament</i>		***
<i>Coming into force</i>	- -	6th April 2008

The Treasury make the following Regulations in exercise of the powers conferred by sections 72C(1), (2) and (3), 72G(1), (2) and (3), and 76(3) of the Building Societies Act 1986⁽⁷⁾.

Citation, commencement and application

24.—(1) These Regulations may be cited as the Building Societies (Accounts and Related Provisions) (Amendment) Regulations 2008.

(2) They come into force on 6th April 2008 and apply in relation to financial years beginning on or after that date.

Amendments to the Building Societies (Accounts and Related Provisions) Regulations 1998

25. The Building Societies (Accounts and Related Provisions) Regulations 1998⁽⁸⁾ are amended as follows.

26. In regulation 10(1), for “the relevant Part” substitute “in the relevant Part”.

27. In Schedule 5 (notes to annual accounts), after paragraph 37 insert—

“Related Party Transactions

38.—(1) Particulars may be given of transactions which the society has entered into with related parties, and must be given if such transactions are material and have not been concluded under normal market conditions.

(2) The particulars of transactions required to be disclosed by sub-paragraph (1) must include—

- (a) the amount of such transactions,
- (b) the nature of the related party relationship,
- (c) other information about the transactions necessary for an understanding of the financial position of the society.

⁽⁷⁾ 1986 c.53. Sections 72C and 72G were substituted, together with sections 72A, 72B, 72D to 72F, and 72H to 72I, for sections 72 and 73 as originally enacted, by S.I. 2004/3380. Regulations made under section 73 have effect as if made under sections 72C and 72G (see article 9(2) of S.I. 2004/3380).

⁽⁸⁾ S.I. 1998/504, as amended by S.I. 2004/3199. There are other amending instruments but none is relevant.

(3) Information about individual transactions may be aggregated according to their nature, except where separate information is necessary for an understanding of the effects of related party transactions on the financial position of the society.

(4) Particulars need not be given of transactions entered into between two or more members of a group, provided that any subsidiary undertaking which is a party to the transaction is wholly-owned by such a member.

(5) In this paragraph, “related party” has the same meaning as in international accounting standards.”.

28. In Schedule 7 (accounting principles and rules), in paragraph 31A—

- (a) in sub-paragraph (2), at the end of paragraph (a), omit “or”;
- (b) at the end of paragraph (b), insert—
“; or
- (c) they are financial instruments falling within sub-paragraph (3A).”;
- (c) in sub-paragraph (3), for “Sub-paragraph (1) does not apply to” substitute “Unless they are financial instruments falling within sub-paragraph (3A) below, sub-paragraph (1) does not apply to”;
- (d) after sub-paragraph (3), insert—

“(3A) Financial instruments which, under international accounting standards adopted by the European Commission on or before 5th September 2006 in accordance with the IAS Regulation, may be included in accounts at fair value, may be so included, provided that the disclosures required by such accounting standards are made.”.

Name

Name

Date

Two of the Lords Commissioners of Her Majesty's Treasury

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Building Societies (Accounts and Related Provisions) Regulations 1998 (S.I. 1998/504) (“the principal Regulations”) to implement in part Directive 2006/46/EC of the European Parliament and of the Council on the annual and consolidated accounts of certain types of companies, banks and other financial institutions (O.J. L 224, 16/8/2006, p.1) (“the Directive”).

Regulation 4 amends Schedule 5 to the principal Regulations, to require societies preparing Building Societies Act accounts to give certain information about transactions with related parties in the notes to those accounts.

Regulation 5 amends Schedule 7 to the principal Regulations, to enable societies preparing Building Societies Act accounts to value a wider range of financial liabilities at fair value in accordance with international accounting standards.

A transposition note showing how the main provisions of the Directive (as it applies to building societies) will be transposed into UK law is available from HM Treasury. Copies may be obtained from the Savings and Investment Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ and the note will be available on the Treasury website (www.hm-treasury.gov.uk).

A full regulatory impact assessment of the effect that this instrument will have on the costs of business is also available from HM Treasury at the above address, and is annexed to the Explanatory Memorandum which is available alongside the instrument on the OPSI website (www.opsi.gov.uk).

 STATUTORY INSTRUMENTS

2008 No. XXXX

FRIENDLY SOCIETIES

The Friendly Societies (Accounts and Related Provisions) (Amendment) Regulations 2008

<i>Made</i>	- - - -	***
<i>Laid before Parliament</i>		***
<i>Coming into force</i>	- -	6th April 2008

The Treasury make the following Regulations in exercise of the powers conferred upon them by sections 69C(1), (2) and (3), 69G(1), (2) and (3), and 121(3) of the Friendly Societies Act 1992⁽⁹⁾.

Citation, commencement and application

29.—(1) These Regulations may be cited as the Friendly Societies (Accounts and Related Provisions) (Amendment) Regulations 2008.

(2) They come into force on 6th April 2008 and apply in relation to financial years beginning on or after that date.

Amendments to the Friendly Societies (Accounts and Related Provisions) Regulations 1994

30.—(1) Regulations 31 to 35 amend the Friendly Societies (Accounts and Related Provisions) Regulations 1994⁽¹⁰⁾.

(2) The Schedule makes consequential amendments to those Regulations.

31. Omit regulation 9 (associated bodies).

32. In Schedule 4 (notes to annual accounts), omit the following paragraphs—

- (a) 3 to 14;
- (b) 30(5) and (6);
- (c) 31.

33. In Schedule 4, after paragraph 34 insert—

“Related Party Transactions

35.—(1) Particulars may be given of transactions which the society has entered into with related parties, and must be given if such transactions are material and have not been concluded under normal market conditions.

⁽⁹⁾ 1992 c.40. Sections 69C and 69G were substituted, together with sections 69A, 69B, 69D to 69F, and 69H to 69I, for sections 69 and 70 as originally enacted, by S.I. 2005/2211. Regulations made under section 70 have effect as if made under sections 69B, 69C, 69F and 69G (see Article 8(2) of S.I. 2005/2211).

⁽¹⁰⁾ S.I. 1994/1983, as amended by S.I. 2005/2210. There are other amending instruments but none is relevant.

- (2) The particulars of transactions required to be disclosed by sub-paragraph (1) must include—
- (a) the amount of such transactions,
 - (b) the nature of the related party relationship,
 - (c) other information about the transactions necessary for an understanding of the financial position of the society.

(3) Information about individual transactions may be aggregated according to their nature, except where separate information is necessary for an understanding of the effects of related party transactions on the financial position of the society.

(4) Particulars need not be given of transactions entered into between two or more members of a group, provided that any subsidiary undertaking which is a party to the transaction is wholly-owned by such a member.

- (5) In this paragraph—

“group” means a society and its subsidiary undertakings;

“related party” has the same meaning as in international accounting standards.”.

34. Omit Schedule 5 (notes to annual accounts: information in respect of associated bodies).

35. In Schedule 6 (accounting principles and rules), in paragraph 24A—

- (a) in sub-paragraph (2), at the end of paragraph (a), omit “or”;
- (b) at the end of paragraph (b), insert—
“; or
- (c) they are financial instruments falling within sub-paragraph (3A).”;
- (c) in sub-paragraph (3), for “Sub-paragraph (1) does not apply to” substitute “Unless they are financial instruments falling within sub-paragraph (3A) below, sub-paragraph (1) does not apply to”;
- (d) after sub-paragraph (3), insert—

“(3A) Financial instruments which, under international accounting standards adopted by the European Commission on or before 5th September 2006 in accordance with the IAS Regulation, may be included in accounts at fair value, may be so included, provided that the disclosures required by such accounting standards are made.”.

Date

Two of the Lords Commissioners of Her Majesty’s Treasury

Name

Name

SCHEDULE

Regulation 30(2)

Consequential amendments to the Friendly Societies (Accounts and Related Provisions) Regulations 1994

36. In regulation 8 (notes to annual accounts)—
- (a) in paragraph (3)(a), omit “a relevant provision of”;
 - (b) omit paragraph (4).
37. In Part III of Schedule 2 (notes on the balance sheet format), in note (4), for “paragraph 5(2) of Schedule 5 below”, substitute “paragraph 5(2) of Schedule 13E to the Act”.
38. In Part III of Schedule 7 (notes to annual accounts of non-directive society), omit paragraphs (b) and (g).
39. In Schedule 9 (interpretation of Schedules)—
- (a) in paragraph 6, omit “(other than paragraphs 4 to 14 and 31 of Schedule 4)”;
 - (b) omit paragraph 9.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Friendly Societies (Accounts and Related Provisions) Regulations 1994 (S.I. 1994/1983) (“the principal Regulations”) to implement in part Directive 2006/46/EC of the European Parliament and of the Council on the annual and consolidated accounts of certain types of companies, banks and other financial institutions (O.J. L 224, 16/8/2006, p.1) (“the Directive”).

Regulations 3, 4 and 6 remove certain provisions of the principal Regulations which relate to disclosures in the notes to societies’ accounts. These disclosures are now required by provisions in the Friendly Societies Act 1992 which were inserted by the Friendly Societies Act 1992 (International Accounting Standards and Other Accounting Amendments) Order 2005 (S.I. 2005/2211).

Regulation 5 amends Schedule 4 to the principal Regulations, to require societies preparing Friendly Societies Act accounts to give certain information about transactions with related parties in the notes to those accounts.

Regulation 7 amends Schedule 6 to the principal Regulations, to enable societies preparing Friendly Societies Act accounts to value a wider range of financial liabilities at fair value in accordance with international accounting standards.

The amendments in the Schedule are consequential on the changes made by regulations 3, 4 and 6.

A transposition note showing how the main provisions of the Directive (as it applies to friendly societies) will be transposed into UK law is available from HM Treasury. Copies may be obtained from the Savings and Investment Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ and the note will be available on the Treasury website (www.hm-treasury.gov.uk).

A full regulatory impact assessment of the effect that this instrument will have on the costs of business is also available from HM Treasury at the above address, and is annexed to the Explanatory Memorandum which is available alongside the instrument on the OPSI website (www.opsi.gov.uk).

Summary: Intervention & Options

Department /Agency: HM Treasury	Title: Impact Assessment of the implementation of Directive 2006/43/EU - Statutory Audit Directive	
Stage:	Version: 1	Date: 27 November 2007
Related Publications:		

Available to view or download at:

<http://www.hm-treasury.gov.uk/consultations>

Contact for enquiries: Sammy Amisshah

Telephone: 020 7270 5291

What is the problem under consideration? Why is government intervention necessary?

To give effect in UK law and to implement Directive 2006/43/EC (the Statutory Audit Directive) - to establish minimum levels of investor protection across the EU by strengthening audit regulation. This will enhance the level of confidence in EU capital markets and whilst these measures may not guarantee the prevention of financial scandals they will mitigate the risks of corporate malpractice occurring.

What are the policy objectives and the intended effects?

The Directive clarifies the duties of statutory auditors and provides for their independence and ethical standards; introduces a requirement for external quality assurance; provides for public oversight of the audit profession, including third party country auditors and increased cooperation between oversight bodies in the EU. It also provides for international cooperation between regulators in the EU and with regulators in third countries.

What policy options have been considered? Please justify any preferred option.

- (a) No intervention.
 - (b) Blanket implementation of the Directive proposals for all entities without taking up Member State exemptions (or distinction to legal form).
 - (c) Implement the Directive by building on the existing UK framework and taking advantage of the flexibilities provided in the Directive, where these are considered to be the preferred policy choice.
- Option C represents the Governments preferred option. It represents the best means of implementation within these flexibilities.

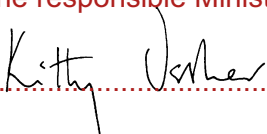
When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

Actual costs and benefits and the achievement of desired effects will be evident after the first reports which are subject to the new requirements are published in 2009. Will be reviewed in 3 years

Ministerial Sign-off Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:



.....Date: 29/11/2007

Summary: Analysis & Evidence

Policy Option:	Description:
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COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' Audit costs incurred for extra disclosure requirements, recording and verifying non audit work performed by accountant for large building societies and friendly societies; Also Government costs relating to policy, legal, printing and distribution of consultation document and implementation.
	One-off (Transition)	Yrs	
	£ 0.01-0.05 million	1	
	Average Annual Cost (excluding one-off)		
£			Total Cost (PV) £ 0.01 - 0.05 million
Other key non-monetised costs by 'main affected groups' Corporate inertia and confusion resulting from a blanket implementation of the Directive's proposals and associated costs of interpreting the provisions.			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' Benefits arising from building society and friendly society members increasing deposits as a direct result of increased confidence following the extra disclosure in their accounts.
	One-off	Yrs	
	£ 7.37 million	3	
	Average Annual Benefit (excluding one-off)		
£ 0.03 million			Total Benefit (PV) £ 28.01 million
Other key non-monetised benefits by 'main affected groups' Enhanced reputation to Government by ensuring that the framework for audit profession and legal framework for societies are up to date.			

Key Assumptions/Sensitivities/Risks Discount Rate of 3.5% based on Green Book. Costs incurred in first year of implementation.

Price Base Year	Time Period Years	Net Benefit Range (NPV) £ 20-27 million	NET BENEFIT (NPV Best estimate) £ 27 million
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What is the geographic coverage of the policy/option?			UK wide		
On what date will the policy be implemented?			6 April 2008		
Which organisation(s) will enforce the policy?			FRC and FSA		
What is the total annual cost of enforcement for these organisations?			£ to be confirmed		
Does enforcement comply with Hampton principles?			Yes		
Will implementation go beyond minimum EU requirements?			No		
What is the value of the proposed offsetting measure per year?			£ to be confirmed		
What is the value of changes in greenhouse gas emissions?			£ N/A		
Will the proposal have a significant impact on competition?			No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		YES	YES	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)	
Increase of	£ N/A	Decrease of	£ N/A	Net Impact £ N/A

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Evidence Base (for summary sheets)

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

1. PROPOSAL

Giving effect in UK law and implementing EC Directive 2006/43 on the Statutory Audit Directive.

2. OBJECTIVE

2.1 The overall objective of this Directive is to clarify the duties of statutory auditors in Member States and to provide for their independence and ethical standards. It also introduces a requirement for external quality assurance; provides for public oversight of the audit profession, including third country auditors and improved cooperation between oversight bodies in the EU.

2.2 The Department for Business, Enterprise and Regulatory Reform (BERR) has already conducted a public consultation on the impact of this Directive on audit firms. The objective of this Impact Assessment is to evaluate the benefits and costs of implementing these measures on the mutual sector. **The Directive will have limited impact on the mutuals sector.**

2.3 Unlike in some Member States, the existing UK framework for statutory audits of entities already provides for a significant proportion of the areas covered by the Directive. Examples include the Directive's proposals on:

- Education and qualifications (Articles 3-14);
- Registration provisions (Articles 15-20);
- Ethics (articles 21-25);
- Standards and reporting (Articles 26-27);
- Public oversight, investigations and discipline (Articles 29-36); as well as
- Cooperation with third country authorities (article 47).

2.4 However there are some areas where specific provision will need to be made in the legislative framework for mutual societies for which the Treasury has policy responsibility (specifically in relation to building societies and friendly societies).

The key elements of this Directive with relevance for the mutuals sector are:

(a) Statutory audits of consolidated accounts

Article 27 of the Directive sets out provisions for the statutory audits of consolidated accounts for groups of undertakings and requires that the auditor bears full responsibility for the audit report in relation to consolidated accounts. This requirement is already provided for in relation to building societies (by section 78(4)(c) of the Building Societies Act 1986 and for friendly societies by section 73 of the Friendly Societies Act 1992. Therefore HM Treasury (HMT) requires no further implementation action for the mutual sector.

(b) Audit reporting

Article 28.1 requires that the statutory auditor to sign the audit report and allow Member States to provide that the name of this person need not be disclosed to the public for security reasons. HM Treasury is aiming to amend the relevant provisions of the Building Societies and Friendly Societies Acts to bring them into line with Companies Act on this point. There are no anticipated costs to societies.

(c) Appointment of auditors

Article 37.1 requires the statutory auditor or audit firm to be appointed by the general meeting of shareholders of the audited entity. Member States may provide for alternative appointment methods provided that the independence of the auditors is not compromised. This provision is already met in relation to building societies by section 77 of and Schedule 11 to the Building Societies Act 1986 and by section 72 of and Schedule 14 to the Friendly Societies Act 1992 so therefore no implementation is required.

(d) Audit reporting

Article 28.1 requires that the statutory auditor to sign the audit report and allows Member States to provide that the name of this person need not be disclosed to the public for security reasons. HMT is proposing to amend the relevant provisions of the Building Societies and Friendly Societies Acts to bring them into line with Companies Act on this point. To facilitate this measure a building society or friendly society must pass a members' resolution and notify the authority of the resolution. There will be costs if a society chooses to correspond with its members specifically in order to implement this requirement. It is expected however that societies will pass such a resolution as part of their Annual General Meeting (AGM) and therefore at no additional cost to societies.

(e) Dismissal and resignation of auditors

Article 38.1 of the Directive requires Member States to ensure that statutory auditors or audit firms are only dismissed where there are proper grounds. Divergence of opinions on accounting treatments or audit procedures shall not be proper grounds for dismissal. This provision is not fully met by the building society and friendly society legislation. The Government therefore proposes to implement this requirement in relation to building societies and friendly societies by introducing a new right to apply to the High court in cases where a society's auditor is alleged to have been removed from office on unfair grounds.

(f) Auditor remuneration for non-audit work

Article 49.1(a) of the Directive requires audited entities to specify separately in the notes to the annual accounts the fees paid to the statutory auditor for non audit work. The existing requirements for building societies and friendly societies on disclosure of auditor remuneration for non-audit work do not meet the requirements of the Directive. The Government proposes to implement this by amending the relevant provisions of the Building Societies Act 1986 and Friendly Societies Act 1992 to bring them in line with company law.

3. BACKGROUND TO DIRECTIVE 2006/43/EC

Directive 2006/43/EC was adopted on 17 May 2006 and published in the Official Journal of the European Communities on 9 June 2006. The purpose of this Directive is "to improve the credibility of financial information and to strengthen protection in the European Union against financial scandals". The full text can be found at www.europa.eu.int

4. OPTIONS APPRAISAL

(a) No intervention. Do nothing to implement the Directive, continuing with the current UK regime, which already reflects many but not all of the provisions in the Directive.

(b) Blanket implementation of the provisions in the Directive without taking up Member State exemptions or taking into account the different legal forms.

(c) Implement the Directive proposals by building on the existing UK framework and taking advantage of the flexibilities provided in the Directive, where these are considered to be the preferred policy choice.

Option C is the Government's preferred option. It represents the most cost effective and efficient means of implementing this Directive taking into account the flexibilities provided.

TABLE OF OPTIONS

See key assumptions, facts and calculations in the Annex

OPTION	COSTS PER ANNUM	BENEFITS PER ANNUM
(a) No intervention	Difficult to quantify but could lead to investor confidence for both building societies and friendly societies.	No benefit to either the building society or friendly society sectors.
(b) Blanket implementation of the provisions in the Directive without taking up Member State exemptions or taking into account the different legal forms.	<p>TOTAL £39,980- £96,000</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • £7,080 to £11,800 <p><u>Friendly Societies</u></p> <ul style="list-style-type: none"> • £2000 to £22,800 <p><u>Government</u></p> <ul style="list-style-type: none"> • £5,000-£10,000 <p><u>Additional administrative costs for societies in applying legislation</u></p> <ul style="list-style-type: none"> • £25,900 - £51,500 	<p>TOTAL £7,372,000</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • Estimated £472, 000. <p><u>Friendly Societies</u></p> <ul style="list-style-type: none"> • £6.9 million <p><u>Government</u></p> <p>No added benefit to Government resulting from the costly and inefficient implementation.</p>
(c) Implement the Directive proposals by building on the existing UK framework and taking advantage of the flexibilities provided in the Directive, where these are considered to be the preferred policy choice.	<p>TOTAL £14080 - £44,600</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • £7,080 to £11,800 <p><u>Friendly Societies</u></p> <ul style="list-style-type: none"> • £2000 to £22,800 <p><u>Government</u></p> <ul style="list-style-type: none"> • £5,000-£10,000 	<p>TOTAL £7,372,000</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • Estimated £472, 000. <p><u>Friendly Societies</u></p> <p>£6.9 million</p> <p><u>Government</u></p> <p>Difficult to quantify but will result in enhanced reputation by ensuring that framework for audit profession and legal framework for societies are up to date</p>

5. RISK, UNCERTAINTY AND UNINTENDED CONSEQUENCES

5.1 The Directive seeks to reduce the risk of future corporate scandals such as WorldCom, Enron, Parmalat by setting out provisions to ensure better regulation of and transparency in the statutory audit function.

5.2 It is difficult to accurately quantify the risk of poor investor confidence across Europe and in the wider global economy resulting from lax audit standards. However it is reasonable to suggest that companies that are embroiled in corporate scandals resulting from negligent audit supervision/checks lose significant market value and are often forced to restructure with subsequent job losses.

5.3 It has been estimated that the loss in stock market wealth in the US as a result of the Enron and WorldCom scandals has been at least 9% or 0.36% of the Gross Domestic Product (GDP)-\$38.2 billion in the first year. (See Graham, Carol/Litan, Robert/Sukhtanker, sandip (2002) “ The bigger they are, the harder they fall: an estimate of the costs of the crisis in corporate governance”.

5.4 A consequence of this is the contagion effect on unrelated businesses that suffer as a result of the wider loss in market confidence.

6. IMPLEMENTATION

6.1 The Directive will be implemented by Orders made under the Building Societies Act 1986, the Friendly Societies Act 1992 and section 2(2) of the European Communities Act 1972.

6.2 HMT is implementing these Directives by, inter alia, amending and providing for the enforcement of certain elements of the regulatory framework that applies to building societies and friendly societies.

7. WHO WILL BE AFFECTED

7.1 The Directives requirements will affect all accountancy firms that carry out statutory audits, and all companies and financial institutions, such as bank and insurance undertakings, which are subject to the requirement to have a statutory audit.

7.2 The Financial Reporting Council is funded by the Government, companies (via listing fees) and the accountancy profession. For Recognised Supervisory Bodies costs will be met on a cost recovery basis via increases in membership fees and therefore falls on auditors and audit firms.

8. EQUITY AND FAIRNESS

8.1 The Government considers that the measures introduced by the Directive will not bring disproportionate benefits or have a disproportionate effect on particular groups.

9. CONSULTATION WITH SMALL BUSINESS

9.1 BERR has held consultative meetings with representative bodies of the audit and accounting profession with a view to assessing the impact of the proposed legislation on the sector.

- **SMALL FIRMS IMPACT TEST (SFIT)**

9.2 The audit Directive applies to those entities that are already subject to statutory audits under the requirements of existing Community law. Under the 4th and 7th Company Law Directives small companies are exempt from the requirements to have a statutory audit providing they meet certain turnover and balance sheet threshold limits. Some small companies, which are not required by law to have their accounts audited, nonetheless elect to do so because they see economic benefits in doing so.

9.3 This SFIT specifically looks at the impact on mutual societies and concludes that it will not have a significant or disproportionate impact on small mutual societies.

• **COMPETITION ASSESSMENT**

9.4 The Directives requirements will affect all accountancy firms that carry out statutory audits, and all companies and financial institutions, such as bank and insurance undertakings, which are subject to the requirement to have a statutory audit.

9.5 It is not expected that the Directive will affect any of these businesses more than others; affect market structure; change the number or sizes of those businesses or lead to higher start-up costs.

10. CONSULTATION

10.1 HMT has discussed the consultation requirements with BERR and the FSA. BERR has in addition discussed the proposed implementing provisions with the Small Business Service and HMRC. The Office of Fair Trading and Companies House have similarly been advised.

10.2 BERR on behalf of Government has discussed the provisions of the Directive with the Financial Reporting Council including the Professional Oversight Board, the Auditing Practices Board, the Financial Reporting Review Panel and the Accounting Standards Board.

10.3 BERR held a public consultation on the provisions of this Directive in July 2007. HMT is now conducting a parallel consultation aimed at informing the mutuals sector, for which it has policy responsibility.

11. ENFORCEMENT AND SANCTIONS

11.1 The Directives provisions will be enforced and monitored by the FSA and the financial reporting Council. The court system will be responsible for sanctions and penalties arising from infringement.

12. SUMMARY AND RECOMMENDATIONS

12.1 The majority of the provisions of the Directive will have to be implemented by 29 June 2008. In line with Government policy on common commencement dates, it is envisaged that the implementing regulations will come into force on 6 April 2008 and will apply to reporting periods on or after that date. Actual costs and benefits and the achievement of the desired effects will be evident after the first reports which are subject to the new requirements are published in 2009.

12.2 Based on our preliminary assessment however the expected benefits of this Directive far outweigh the costs and is recommended. We also recommend a post implementation review in 3 years time to establish whether the implemented regulations are having the intended effect and to ascertain whether there are any unintended effects, which will need to be addressed.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No

Annexes

A

OPTION	TOTAL COSTS	TOTAL BENEFITS
A	N/A	N/A
B	£39,980 - £96,100	£7,372,000 *
C	£14,080 - £44,600	£7,372,000

Same quantifiable benefits however more costly.

B

PRESENT VALUE CALCULATIONS

BENEFITS (OPTION C)

	Year	Discount factor	Benefit
To	2007	3.5%	£7.37 million
T1	2008	3.5%	£7.12 million
T2	2009	3.5%	£6.88 million
T3	2010	3.5%	£6.64 million

TOTAL BENEFIT (PRESENT VALUE): £28.01 million

C.

AVERAGE ANNUAL BENEFIT EXCLUDING ONE-OFF BENEFIT

$(£28.01 - £7.37) / 3 \text{ YEARS} = £6.88 \text{ million}$

$£6.88 \text{ million} / 259 \text{ societies} = \mathbf{£26,563}$

D.

Some key assumptions and facts

Staff and Production Costs

- Month's salary costs for policy staff and legal teams in researching, drafting, publishing consultation document and implementing legislation.

Building societies

- **59 Building societies** in the UK as at 1 November 2007.
- Main costs associated with the extra disclosure requirement for audited entities to specify separately in the notes to the annual accounts the fees paid to the statutory auditor for non-audit work.
- Based on 4 hours work for accountant. Hourly rates of £30 per hour for Small Enterprises and £50 per hour for Medium – Large.

Friendly Societies

- Analysis based on 200 friendly societies and total membership of 6.9 million as at 1 January 2007.
- Based on 4 hours work for accountant. Hourly rates of £30 per hour for Small Enterprises and £50 per hour for Medium – Large.
- In terms of funds under management the friendly society sector is highly concentrated with the top 10 societies accounting for just 90% of the total net assets as well as membership.
- The Directive's requirements will potentially benefit the mutual societies (building societies and friendly societies). It would increase transparency in their accounts making it easier for investors to make informed decisions. It would also mean that their accounts are subject to the same rigour and scrutiny as their EU counterparts.
- It is difficult at this stage to provide a precise quantification of the benefits and costs associated with this Directive as it is uncertain how or when these (especially the benefits) would take effect. It is also unlikely that the benefits would be felt by all societies instantaneously. It is more likely to have a staggered impact with the initial impact possibly felt by the largest societies.

OPTION A (Cost/Benefit comparison)

- There are no benefits to failing to implement this Directive. On the contrary building societies and friendly societies would suffer from a lack of investor confidence. The audit profession would also suffer a credibility gap, as their legislative framework would not be abreast with EU standards. It would also put the UK at risk of infraction proceedings from the EU.

OPTION B (Cost/Benefit comparison)

Building societies

- The main effect of this Directive is that audited entities would need to specify separately in the notes to the annual accounts the fees paid to the statutory auditor for non audit work. It is likely that the auditor will need to perform extra checks to ensure that (a) all non-

audit work have been disclosed and (b) that the work has been correctly valued at arm's length valuations. This may require an independent auditor other than the one who had performed the services in question.

- Costs based on ½ day's work for an accountant.
- **Small Building Society: £30 x 4 hours x 59 = £7,080**
- **Medium to large Building Society: £50 x 4 hours x 59 = £11,800**

Benefits: Based on a conservative estimate that if each of 472,000 depositors increased their deposits by £1 directly as a result of increased confidence in the building society sector. **(£472,000)**

Friendly societies

- The costs are based on ½ day's work for an accountant.
- Top 10 incurring additional costs of £200 each and remaining 190 incurring additional costs of £120 each
- **Large Friendly Society: £50 x 4 hours x 10 = £2000**
- **Small to Medium Friendly Society: £30 x 4 hours x 190 = £22,800**

Estimated benefits: Even if the 6.9 million members increased their deposits by a marginal £1 as a direct result of increased confidence = **(£6.9 million)**.

Additional costs for societies

Extra time resources in interpreting legislation to apply to the affected mutual societies with each society incurring between £100 and £200. Costs in relation to staff and cash resources expended on **reformatting the Directive requirements to fit the needs of societies. (£25,900 - £51,500)**

Government costs

Comprising of staff costs (including legal) in researching, drafting, publishing consultation document and implementing legislation. **£5,000 to £10,000.**

OPTION C (Cost/benefit comparison)

Building Societies

- The main effect of this Directive is that audited entities would need to specify separately in the notes to the annual accounts the fees paid to the statutory auditor for non audit work. It is likely that the auditor will need to perform extra checks to ensure that (a) all non-audit work have been disclosed and (b) that the work has been correctly valued at arm's length valuations. This may require an independent auditor other than the one who had performed the services in question.
- Costs based on ½ day's work for an accountant.
- **Small Building Society: £30 x 4 hours x 59 = £7,080**
- **Medium to large Building Society: £50 x 4 hours x 59 = £11,800**
- In contrast the benefits of transparency and increased investor confidence would be immense. Even on a very conservative estimate if the 472, 000 depositors increased

their deposits by just £1 each directly as a result of increased confidence this would equal **£472,000**.

- **472,000 members x £1 = £472,000**

Friendly Societies

- The costs are based on ½ day's work for an accountant.
- Top 10 incurring additional costs of £200 each and remaining 190 incurring additional costs of £120 each
- **Large Friendly Society: £50 x 4 hours x 10 = £2000**
- **Small to Medium Friendly Society: £30 x 4 hours x 190 = £22,800**
- In contrast the benefits of transparency and increased investor confidence would be immense. There were 6.9 million members as at 31 December 2006.

Even based on a conservative estimate if the 6.9 million members increased their deposits by a marginal £1 as a direct result of increased confidence = **(£6.9 million)**.

Summary: Intervention & Options

Department /Agency:
HM Treasury

Title:
Impact Assessment of Directive 2006/46/EC on
Company Reporting- Amending the Accounting
Directives

Stage:

Version: 1

Date: 27/11/2007

Related Publications:

Available to view or download at:

<http://www.hm-treasury.gov.uk/consultations>

Contact for enquiries: Sammy Amissah

Telephone: 020 7270 5291

What is the problem under consideration? Why is government intervention necessary?

To give effect in UK law and to implement Directive 2006/46/EC on Company Reporting-amending the 4th and 7th Accounting Directives-to reduce the risk of future corporate scandals and the adverse impact on investor confidence.

What are the policy objectives and the intended effects?

To further enhance confidence in the financial statements and annual accounts published by mutual societies (building societies and friendly societies) allowing members and stakeholders to make comparable assessments of different societies across borders by having access to complete and reliable information in relation to their financial arrangements and corporate governance.

What policy options have been considered? Please justify any preferred option.

(a). No intervention.

(b). Blanket implementation of the provisions in the Directive for all entities without taking up Member State exemptions (or distinction to legal form).

(c). Implement the provisions in the Directive for mutual societies which fall within the scope of the Directive taking up all Member State exemptions and taking into account the different legal form.

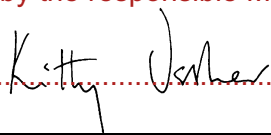
Preferred options C - there are distinct differences between mutual societies and companies, which need to be reflected in the implementation proposals. Taking up exemptions gives UK flexibility.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Date to be confirmed. But at least 3 years after implementation.

Ministerial Sign-off Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

.....

Date: 3/12/2007

Summary: Analysis & Evidence

Policy Option:	Description:
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COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' Additional disclosure costs for large building societies and friendly societies in respect of annual corporate governance statement, related party and off-balance sheet transactions. Also Government costs relating to policy, legal, printing and distribution of consultation document and implementation.
	One-off (Transition)	Yrs	
	£0.02-0.12mn	1	
	Average Annual Cost (excluding one-off)		
£		Total Cost (PV)	£0.02-0.12mn
Other key non-monetised costs by 'main affected groups' Corporate inertia and confusion arising from a blanket implementation of the Directive's proposals and associated costs of interpreting the provisions.			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' Benefits arising from building society and friendly society members increasing deposits as a direct result of increased confidence following the extra disclosure in their accounts.
	One-off	Yrs	
	£7.37 mn	3	
	Average Annual Benefit (excluding one-off)		
£ 0.03 mn		Total Benefit (PV)	£ 28.01mn
Other key non-monetised benefits by 'main affected groups' Increased investor confidence will attract additional investment.			

Key Assumptions/Sensitivities/Risks Key assumptions: Discount Rate of 3.5% based on Green Book. Costs incurred in the first year of implementation approximately 1 day's work (8 hours) for accountant at £30-£50 per hour. Benefits are amortised over 3 years. Discount period is assumed to be 3 years, (when policy will be reviewed).

Price Base Year 2007	Time Period Years 3	Net Benefit Range (NPV) £ 20-27 mn	NET BENEFIT (NPV Best estimate) £ 27 mn
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What is the geographic coverage of the policy/option?		UK wide		
On what date will the policy be implemented?		06 April 2008		
Which organisation(s) will enforce the policy?		FSA		
What is the total annual cost of enforcement for these organisations?		£ to be confirmed		
Does enforcement comply with Hampton principles?		Yes		
Will implementation go beyond minimum EU requirements?		No		
What is the value of the proposed offsetting measure per year?		£ to be confirmed		
What is the value of changes in greenhouse gas emissions?		£ N/A		
Will the proposal have a significant impact on competition?		No		
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)		(Increase - Decrease)		
Increase of	£ N/A	Decrease	£ N/A	Net Impact £ N/A

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Evidence Base (for summary sheets)

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

1. PROPOSAL

1.1 The Directive 2006/46/EC (“the Directive”) of the European Parliament and Council was published on 16th August 2006. The proposal aims to give effect in UK law and to implement this Directive. The full text of the Directive can be found at www.europa.eu.int

1.2 The Directive amends Council Directives:

- 78/660/EC on the annual accounts of certain types of companies (“the Fourth Directive”),
- 83/349/EEC on consolidated accounts (“the Seventh Directive”),
- 86/635/EEC on the annual accounts and consolidated accounts of banks and other financial institutions (“the bank Accounts Directive”)
- 91/674/EEC on the annual accounts and consolidated accounts of insurance undertakings (“the Insurance Accounts Directive”).

2. OBJECTIVE

2.1 The Directive seeks to “further enhance confidence in the financial statements and annual reports published by European companies to provide shareholders and other stakeholders (e.g. employees and suppliers) with reliable, complete, and easily accessible information”.

2.2 In order to achieve its overall objective the Directive contains six revisions to the 4th and 7th Directives and the Bank Accounts and Insurance Accounts Directives, five of which require, or contain a Member State option to permit, changes to the relevant UK company law.

(a) Raising the financial thresholds used to define small and medium sized companies for accounting and reporting purposes.

This option is not relevant to building societies or friendly societies.

(b) Extended use of Fair Value Accounting

This Member State option will be applicable to all building societies and friendly societies that choose to adopt fair value accounting for financial instruments and associated disclosures.

(c) Enhancing transparency about off-balance sheet arrangements.

This will apply to friendly society insurers falling within the scope of the insurance Directives and to building societies.

(d) Enhancing transparency about related party transactions

This will apply to building societies and friendly societies that prepare their accounts under the Building Societies or Friendly Societies Acts rather than in accordance with international accounting standards.

(e) Introducing an annual corporate governance statement

The only building societies and friendly societies affected by this provision will be those whose securities are traded on a regulated market.

3. BACKGROUND TO DIRECTIVE 2006/46/EC

3.1 As part of the European Commission's broader programme of company law reform it published an Action Plan in May 2003 containing some legislative measures aimed at enhancing the credibility of financial statements and annual reports published by European Companies.

3.2 The Directive focuses on linked objectives of increasing confidence in corporate governance frameworks and improving investor confidence through increased transparency and better information on companies.

3.3 The measures in the Directive contribute to several of the aims of that the Government believes are important to industry, namely:

- increased financial stability and market confidence
- extending investment opportunities across the EU
- improving access to capital by companies across borders.

3.4 Research by academics including "The Benefits of Transparency" by Christian Leuz, Capital Ideas Journal, July 2006 and "International Differences in the Cost of Equity Capital", by Hail, Luzi and Leuz, December 2005 - concludes that there is a link between transparency and cost of capital of certain institutions. They found that firms from countries with more extensive disclosure requirements, stronger securities regulation and stricter enforcement mechanisms (as enabled by a high quality legal infrastructure) had significantly lower cost of capital.

3.5 This is because where there are increased disclosure requirements, investors are better placed to assess the risks and benefits of their investments and so enable them to make more efficient investment decisions.

3.6 The requirements of this Directive are broadly consistent with existing UK law and practice. Informal stakeholder soundings in response to the proposals indicate that Government should support its broad principles. The Department for Business Enterprise and Regulatory Reform (BERR) has met with representatives and stakeholders of entities affected by the Directive to discuss the implementation proposals.

4. OPTIONS APPRAISAL

(a) No Intervention

Not doing anything may put mutual societies in the UK in a disadvantageous position in relation to their EU counterparts and would breach UK's obligations under the EC Treaty. This option would therefore have limited economic effect but would cause difficulties in the future.

(b) Blanket implementation of the provisions in the Directive for all entities, without taking up Member State exemptions (or distinction to legal form).

Implementing the Directive requirements without taking up the exemptions or distinction to the legal form to create a "one size fits all" situation would not be beneficial or practical. There are distinct differences between the various legal forms with their specific audit reporting and corporate governance requirements

(c) Implement the provisions in the Directive for mutual societies, which fall within the scope of the Directive taking up all exemptions and tailored to meet the specificities of the mutual form.

This option would enable an optimal application of the Directive to reflect the differences in legal form and ensure that the Directive requirements are applied in an effective and proportionate manner to suit each type of legal form and mutual society.

4.1 The Government's preferred option is C - there are distinct differences between mutual societies and proprietary companies, which needs to be reflected in the implementation proposals.

TABLE OF OPTIONS

See key assumptions, facts and calculations in the Annex.

OPTION	COST PER ANNUM	BENEFIT PER ANNUM
(a) No Intervention	Difficult to quantify but could lead to loss of investor confidence for both building societies and friendly societies.	No benefit to either the building society or friendly society sectors.
(b) Implement the provisions in the Directive for all entities, which fall within the scope of the Directive (without taking up exemptions or distinction to legal form)	<p>TOTAL £49,060 - £121,700</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • £14,160 - £23,600 <p><u>Friendly Societies</u></p> <ul style="list-style-type: none"> • £4000 - £45,600 <p><u>Government</u></p> <ul style="list-style-type: none"> • £5,000 - £10,000 <p><u>Additional implementation costs</u></p> <ul style="list-style-type: none"> • £25,900 - £51,500 	<p>TOTAL £7,372,000</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • Benefits of £472,000 <p><u>Friendly societies</u></p> <ul style="list-style-type: none"> • Benefits of £6.9 million <p><u>Government</u></p> <ul style="list-style-type: none"> • Not quantifiable
(c) Implement the provisions in the Directive only for mutual societies, which fall within the scope of the Directive taking up all exemptions.	<p>TOTAL £23,160 - £89,200</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • £14,160 - £23,600 <p><u>Friendly Societies</u></p> <ul style="list-style-type: none"> • £4000 - £45,600 <p><u>Government</u></p> <p>£5,000 - £10,000</p> <p>Plus £10,000 for annual corporate governance</p>	<p>TOTAL £7,372,000</p> <p><u>Building Societies</u></p> <ul style="list-style-type: none"> • Benefits of £472,000 <p><u>Friendly societies</u></p> <ul style="list-style-type: none"> • Benefits of £6.9 million <p><u>Government</u></p> <ul style="list-style-type: none"> • Not quantifiable

	statement for the 20 or so largest building societies, which have listed securities and traded, subordinated debt.	
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5. RISK, UNCERTAINTY AND UNINTENDED CONSEQUENCES

5.1 The provisions in this Directive arose because the Commission had concerns that investor confidence had been badly compromised following the recent corporate scandals such as WorldCom, Enron and Parmalat. The Commission's view was that making financial arrangements more transparent and requiring companies to give information relevant to good corporate governance would reduce the risk of future corporate scandals in Europe.

5.2 Analysis of the loss in investor confidence based on the fall in stock market wealth following the failure of Enron and WorldCom in July 2002 was estimated at 0.36% of Gross Domestic Product or \$38.2 billion in the first year. (See Graham, Carol/Litan, Robert/Sukhtanker, Sandip 2002) - The bigger they are, the harder they fall: an estimate of the costs of the crisis in corporate governance".

5.3 It is therefore imperative that any reasonable steps that are taken by the Commission to mitigate this risk are treated constructively. An unintended consequence of this Directive is that the smallest mutual societies will be required to provide the same level of detailed information as the larger ones. This will however ensure comparability between societies irrespective of size or physical location within the European Union.

6. IMPLEMENTATION

The Directive will be implemented by Orders made under the Building Societies Act 1986, the Friendly Societies Act 1992 and section 2(2) of the European Communities Act 1972.

7. WHO WILL BE AFFECTED?

7.1 This Directive will affect companies, partnerships, building societies and those friendly societies and industrial & provident societies covered by the Insurance Accounts Directive, and other institutions covered by the Bank Accounts directive. The HMT consultation is specifically aimed at building societies and friendly societies. The other entities are already covered by the BERR consultation and implementation procedures. The changes will apply in relation to financial years commencing on or after 6 April 2008.

8. EQUITY AND FAIRNESS

8.1 The Government considers that the measures introduced by the Directive will not have a disproportionate impact on the groups identified.

9. CONSULTATION WITH SMALL BUSINESS

- **SMALL FIRMS IMPACT TEST**

9.1 BERR has held consultative meetings with some representative groups in the mutual sector with a view to assessing the impact of the proposed legislation on small firms. The Government view is that only the very largest businesses would be impacted on by the Directive requirements. For example only the largest societies would have/find the need to

engage in substantial off-balance sheet transactions. Accordingly it is Government's view that there will not be a disproportionate impact on small business.

- **COMPETITION ASSESSMENT**

9.2 We have carried out a competition filter test and concluded that the Directive has a potential impact on UK building societies and friendly societies. It was considered that the Directive would not give rise to disproportionate costs of entry or administrative costs for either small or larger societies. The Directive is not expected to restrict innovation in sectors characterised by rapid technological change and would not impair the freedom to provide services.

10. CONSULTATION

10.1 HMT has discussed the consultation requirements with BERR and the FSA. BERR has in addition discussed the proposed implementing provisions with the Small Business Service and HMRC. The Office of Fair Trading, Companies House have also been informed.

10.2 BERR on behalf of Government has discussed the provisions of the Directive with the Financial Reporting Council including the Professional Oversight Board, the Auditing Practices Board, the Financial Reporting Review Panel and the Accounting Standards Board.

10.3 BERR held a public consultation on the provisions of this Directive as applicable to certain types of companies from 5 March 2007 to 7 June 2007. HMT is now conducting a parallel consultation in respect of mutual societies for which it has policy responsibility (building societies and friendly societies).

11. ENFORCEMENT AND SANCTIONS

11.1 The bodies responsible for monitoring and enforcing sanctions are the Financial Services Authority and the Courts. We believe that the organisations involved together have the necessary powers to monitor and enforce the Directive requirements.

12. SUMMARY AND RECOMMENDATIONS

12.1 The Government is required to implement this EC Directive by the deadline of 5 September 2008. It aims to do this in an effective and proportionate manner without imposing extra burdens on societies affected. The implementation proposals suggested in the consultation document, the Members State options exercised by the Government as well as the implementation option adopted would ensure that these objectives are achieved in a cost effective and efficient manner.

12.2 The expected benefits of this Directive far outweigh the costs and is recommended.

12.3 We also recommend a post implementation review in 3 years time to establish whether the implemented regulations are having the intended effect and to ascertain whether there are any unintended effects, which will need to be addressed.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No

Annexes

A

OPTION	TOTAL COSTS PER ANNUM (BUILDING SOCIETIES & FRIENDLY SOCIETIES)	TOTAL BENEFITS PER ANNUM (BUILDING SOCIETIES & FRIENDLY SOCIETIES)
A	N/A	N/A
B	£49,060 - £121,700	£7,372,000*
C	£23,160 - £ 89,200	£ 7,372,000

* Same quantifiable benefits, however more costly.

B

PRESENT VALUE CALCULATIONS

BENEFITS (OPTION C)

	Year	Discount factor	Benefit
To	2007	3.5%	£7.37 million
T1	2008	3.5%	£7.12 million
T2	2009	3.5%	£6.88 million
T3	2010	3.5%	£6.64 million

TOTAL BENEFIT (PRESENT VALUE): **£28.01 million**

C

AVERAGE ANNUAL BENEFIT EXCLUDING ONE-OFF BENEFIT

(£28.01 million - £7.37) / 3 years= £6.88 million

£6.88 million / 259 societies= **£26,563**

D

Some key assumptions and facts

Building Societies:

- **59 Building Societies** in the UK as at 1 November 2007
- Accountant's fees per 8-hour day (£240 - £400). Based on hourly rates of £30 per hour for Small Enterprises and £50 per hour for Medium – Large.

Friendly Societies:

- Analysis based on **200 friendly societies** and total membership of 6.9 million as at 1 Jan 2007.
- Accountant's fees per 8-hour day (£240 - £400). Based on hourly rates of £30 per hour for Small Enterprises and £50 per hour for Medium – Large.
- Although more than 2000 societies registered as various classes of societies under the Friendly Societies Acts little more than 200 of them are regulated by the Financial Services Authority under the Financial Services and Markets Act 2000.
- In terms of funds under management the friendly society sector is highly concentrated with the top 10 societies accounting for just over 90% of the total net assets as well as membership.
- The Directive's proposals will potentially benefit all the mutual societies (building societies, friendly societies) affected. It would increase transparency in the accounts making it easier for investors to make informed decisions.
- It is difficult at this stage to provide a precise quantification of the benefits and costs associated with this Directive, as it is uncertain as to when these benefits would take effect. It is unlikely that the benefits would be felt by all societies instantaneously. It is more likely to have a staggered impact.

OPTION A (Cost/Benefit comparison)

- There are no benefits to failing to implement this Directive. On the contrary mutual societies in the UK would suffer from investor confidence and inability to make like with like comparisons with societies in other Member States.

OPTION B (Cost/Benefit comparison)

Building societies

- There are currently 59 building societies in the UK. Implementing the Directive requirements could entail additional reporting on the use of Fair Value Accounting, off-balance sheet arrangements, related party transactions and annual corporate governance statement.

Costs based on accountants fee for day's work.

Small building society: £240 x 59 = **£14,160**

Medium to large building society: £400 x 59 = **£23,600**

- In contrast the benefits of transparency and increased investor confidence would be immense. Even on a very conservative estimate if the 472,000 depositors increased their deposits by just £1 directly as a result of increased confidence this would equal **£472,000**

Friendly Societies

- There are 200 Friendly Societies. The costs are based on accountant's fee for day's work.

Top 10 each incurring additional costs of £400 and remaining 190 incurring £240 each.

Large Friendly Society: 10 x £400 = **£4,000**

Medium to large Friendly Society: 190 x 240 = **£45,600**

- In contrast the benefits of transparency and increased investor confidence would be immense. There were 6.9 million members as at 31 December 2006. Even based

on a conservative estimate if the total membership increased their deposits by a **marginal £1** this would be **equal to £6.9 million**

Government

- Government costs for policy research, legal drafting, publishing and distribution of consultation document estimated to be around **£5,000 to £10,000**

Additional Costs by all 259 societies (building and friendly societies)

Resulting from extra time resources in interpreting legislation to apply to Mutuals with each society incurring £100 - £200. **(£25,900 - £51,500)**

OPTION C (Cost/ Benefit comparison)

Building Societies:

- There are currently 59 building societies in the UK. Implementing the Directive requirements could entail additional reporting on the use of Fair Value Accounting, off-balance sheet arrangements, related party transactions and annual corporate governance statement.

Costs based on accountants fee for day's work.

Small building society: £240 x 59 = **£14,160**

Medium to large building society: £400 x 59 = **£23,600**

- **PLUS** an additional £500 each for the 20 Building Societies, which have listed securities and traded subordinated debt and will therefore need to have an annual corporate governance statement **(£10,000)**.
- In contrast the benefits of transparency and increased investor confidence would be immense. Even on a very conservative estimate if the 472,000 depositors increased their deposits by just £1 directly as a result of increased confidence this would equal **£472,000**

Friendly societies:

- Costs based on top 10 each incurring additional costs of £400 and remaining 190 incurring £240 each.

Large Friendly Society: 10 x £400 = £4,000

Medium to Large Friendly Society: 190 x 240 = £45,600

- In contrast the benefits of transparency and increased investor confidence would be immense. There were 6.9 million members as at 31 December 2006. Even based on a conservative estimate if the total membership increased their deposits by a **marginal £1** this would be **equal to £6.9 million**

Government

- Government costs for policy research, legal drafting, publishing and distribution of consultation document estimated to be around **£5,000 to £10,000**

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