Department of Trade and Industry

INTERNATIONAL ACCOUNTING

STANDARDS

A CONSULTATION DOCUMENT

ON THE POSSIBLE EXTENSION OF THE EUROPEAN REGULATON ON INTERNATIONAL ACCOUNTING STANDARDS

30 August 2002

URN 02/1158

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1. SUMMARY AND QUESTIONS

1.1 The Regulation of the European Parliament and of the Council on the Application of International Accounting Standards was adopted by Member States on 7 June 2002. It applies from the financial years commencing 1 January 2005. The Regulation and an explanatory note are attached at Annexes A and B respectively.

1.2 The Regulation introduces important changes, which will directly affect the way in which certain companies across the European Union (EU) prepare their financial statements. As a minimum, it will require companies governed by the law of a Member State, whose securities are admitted to trading on a regulated market in any Member State in the European Union ("**publicly traded companies**"), to prepare their consolidated accounts on the basis of accounting standards issued by the International Accounting Standards Board (IASB) that are adopted by the European Commission. Annex C provides a list of regulated markets in the EU. An explanation of the adoption process is included at Annex B. Current standards are known as International Accounting Standards (IAS). Future standards will be known as International Financial Reporting Standards. The Regulation only applies to the detailed accounting provisions; domestic law implementing the Accounting Directives where relevant will continue to apply in other areas such as the requirement to prepare accounts, auditing, enforcement and the directors' report.

1.3 This is a significant development in financial reporting. The Government welcomes the adoption of the Regulation and strongly supports the European move to use IASB standards. Global markets require high quality globally agreed accounting standards to work more effectively. For publicly traded companies, adherence to global accounting standards should help to reduce the cost of capital by making their accounts more accessible to potential investors across the EU and worldwide. For potential investors, creditors and other users of financial statements, global standards provide a single means by which to compare performance and prospects on a like-for-like basis. Global standards should also help to promote financial stability.

1.4 For those UK companies affected, the Regulation will have two main impacts. Firstly, they will have to comply with adopted accounting standards issued by the IASB, in place of much of the Companies Act 1985 and the domestic accounting standards issued by the Accounting Standards Board (ASB) (which are in any case converging with IAS - see paragraphs 3.8-3.11). Secondly, those standards will have direct legal force. The same conditions will apply to relevant companies in the other Member States. It is important that companies covered by the Regulation and their accountants and auditors begin planning ahead for the change, if they are not already doing so.

1.5 As noted, the Regulation applies directly to the consolidated accounts of publicly traded companies. It also gives each Member State certain options to extend its application (and hence the need to comply with adopted IAS). Each Member State may permit or require:

- publicly traded companies to prepare their individual accounts in accordance with adopted IAS;

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

1.6 The Regulation also gives each Member State the option of delaying its application until 1 January 2007 in the case of:

- publicly traded companies which have only their debt securities (eg bonds) admitted on an EU regulated market;

- publicly traded companies whose securities are admitted to trading on markets outside the EU and which, for that purpose, currently use internationally accepted accounting standards (eg US standards).

1.7 The purpose of this consultation is twofold: to explain the background to the Regulation, what it means and how it will work (section 3, Annex B); and to seek views on the Member State options in paragraphs 1.5 and 1.6 (section 4). It should be noted that the consultation does not consider the mandatory application of the Regulation to the consolidated accounts of publicly traded companies - the Regulation in this respect has already been adopted by the European Parliament and the Council of Ministers.

1.8 The Government does not yet have a preferred option on the extension of the application of the Regulation beyond the consolidated accounts of publicly traded companies.

1.9 The Government does not believe there is a case for deferring application of the Regulation until 2007 for the companies mentioned in paragraph 1.6.

1.10 The Government expects to come to a decision on the options early next year in the light of this consultation.

1.11 This consultation is separate from the general consultation being carried out in parallel on reform of company law in Great Britain ("Modernising Company Law", Cm 5553-1, published 16 July 2002, www.dti.gov.uk/companiesbill/whitepaper.htm). However, the two are closely linked in some respects, since any extension of the application of the Regulation (and hence the application of adopted IAS) could have implications for the White Paper's proposals on a new institutional framework for domestic accounting requirements (see paragraphs 3.20-3.21).

1.12 Limited Liability Partnerships (LLPs), and undertakings that are prudentially regulated under the Financial Services and Markets Act 2000 (FSMA) and do not have the status of companies, are not covered by the Regulation or its options, and so are not strictly part of this consultation. However, the Government will need to consider their position in relation to IAS once it has decided on the exercise of the Member State options. The Government's general policy on such bodies is to treat them in the same way as companies of the same size and sector unless this is clearly inappropriate. The Government is taking advantage of the consultation to inform any consequential decisions relating to LLPs and other undertakings. Some of the bodies are the responsibility of HM Treasury rather than DTI.

Questions for consideration

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

1. Should the Government extend the application of the Regulation beyond the requirement for the consolidated accounts of publicly traded companies to comply with adopted IAS? (see paragraphs 4.4 - 4.10)

2. If you think that the Regulation should be extended, do you consider that this should be:

(a) on a voluntary basis whereby the Government permits some or all companies to comply with adopted IAS?

(b) on a compulsory basis whereby the Government requires some or all companies to comply with adopted IAS?

(see paragraphs 4.11 – 4.14)

3. If you think that the Regulation should be extended in the UK, to which accounts and companies do you think the extension should apply:

(i) the individual accounts of publicly traded companies?

(ii) the individual accounts of the subsidiaries of publicly traded companies?

(iii) the individual accounts of publicly traded companies that do not produce consolidated accounts?

(iv) the individual and/or consolidated accounts of large and medium sized non-publicly traded companies, eg all companies above those small companies that could apply the ASB's FRSSE?

(v) the individual and/or consolidated accounts of all companies?

(vi) the individual and/or consolidated accounts of companies that are prudentially regulated under FMSA?

(see paragraphs 4.15 – 4.28)

4. Do you consider that application of the Regulation should be deferred until 1 January 2007 for:

(a) publicly traded companies, which have only their debt securities (eg bonds) admitted on a regulated market in the EU?

(b) publicly traded companies whose securities are admitted to trading on markets outside the EU and which use internationally accepted accounting standards?

(see paragraphs 4.29 – 4.32)

5. Can you:

(a) identify any costs or savings for your company or more generally resulting from the above options for extension or delay of the application of the Regulation and hence the application of adopted IAS?

(b) quantify those costs or savings?

(see paragraph 4.33)

You may wish say what impact the ASB's ongoing convergence programme (designed to bring UK accounting standards into line with IASB standards) might have on these costs or savings.

6. Should LLPs, and undertakings that are prudentially regulated under FSMA and do not have the status of companies, also be permitted or required to prepare their accounts in accordance with adopted IAS, on the same basis as companies of the same size and sector? (Note that this could not be done as part of this exercise, but would have to be done separately.) (see paragraphs 4.34 – 4.36)

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

2. HOW TO REPLY

2.1 We invite comments by **26 November 2002** at the latest. Earlier responses would be very welcome.

2.2 Responses should be sent - by email if possible - to:

IAS Consultation Document
Company Law and Investigations Directorate
Department of Trade and Industry
Bay 4101
1 Victoria Street
London SW1H 0ET

Fax: **020 7215 0235**

E-mail: **iasconsultation@dti.gsi.gov.uk**

2.3 All responses will be acknowledged. In accordance with the code of practice on open government, comments will be made publicly available unless respondents specifically request otherwise.

Additional copies

2.4 This document is available electronically at www.dti.gov.uk/consultations. You may also photocopy it if you wish, or additional hard copies may be obtained by calling 020 7215 0232.

Questions

2.5 If you have questions about the issues discussed in this consultation document, please phone Valerie Carpenter on 020 7215 0225.

3. BACKGROUND

Development of the Regulation

3.1 During 1999, the European Commission published a communication on "*Financial Services: Implementing the Framework for Financial Markets: Action Plan*". In March 2000, Ministers of Member States at the Lisbon European Council concluded that, in order to accelerate completion of the internal market for financial services, steps should be taken to enhance the comparability of companies' financial statements by 2005.

3.2 Consequently, in February 2001 the European Commission published a proposal for a Regulation on the application of IAS in the EU, as a key element of its Financial Services Action Plan. It aimed to harmonise financial reporting in the EU on the basis of globally agreed accounting standards by 2005.

3.3 The Regulation was adopted on 7 June 2002. It requires publicly traded companies governed by the law of a Member State to prepare their consolidated accounts on the basis of accounting standards issued by the IASB and adopted by the European Commission, from 1 January 2005.

3.4 The UK was closely involved in negotiations on the Regulation. The Government welcomes its adoption and strongly supports the European move to use IASB standards.

International Accounting Standards Board

3.5 The IASB is an independent body, formed in 2001 to succeed the International Accounting Standards Committee. That body was formed in 1973 through an agreement made by professional accountancy bodies from Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom and the United States of America. It is committed to developing, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require transparent and comparable information in general purpose financial statements. It has formal links with standard setters in a number of countries, including the ASB.

3.6 For each standard, the IASB is expected to publish a discussion document setting out various possible requirements with arguments for and against. It will then publishes a draft standard for public comment, and subsequently decide on the final form of the standard. Draft and final standards can only be issued with the agreement of a majority of the Board's fourteen members. IASB standards tend to be focussed on large publicly traded companies.

3.7 Currently the IASB is engaged in a substantial exercise to upgrade the quality of its standards. It has a full programme of major projects, which are expected to lead to revisions of most of its existing standards both up to and beyond 2005. In two recent exposure drafts it has already proposed improvements to fourteen standards. Further information on the IASB is available from its website, www.iasb.org.uk.

The ASB's convergence programme

3.8 In the UK, the ASB's accounting standards apply to all UK companies and are also used by a variety of other entities. The ASB and IASB standards are in many cases very similar, although there are also a number of differences. In the light of the prospective adoption of IAS within the EU for some companies, the ASB is concentrating its efforts on achieving convergence between UK accounting standards and IASB standards. The timeframe within which the ASB might be able to achieve convergence of all UK standards with IASB standards is heavily dependent on how quickly the IASB's projects advance, and the extent to which the IASB further reconsiders standards to which it has already proposed improvements. Further information on the ASB is available from its website, www.asb.org.uk.

3.9 The ASB has indicated that it will be mindful of the implications for non-publicly traded companies of using an accounting framework that is designed for the global capital market, with a view to avoiding unnecessarily onerous requirements on such companies.

3.10 For certain types of company, UK accounting standards sustain a reporting regime that is more specific than IASB standards. Examples are charities and investment trusts. In both these sectors, companies comply with a Statement of Recommended Practice (SORP), which is also followed by non-corporate reporting entities. A SORP gives guidance on the application of UK accounting standards in the circumstances of particular industries or sectors. IASB standards do not currently include a reporting structure attuned to the needs of these sectors.

3.11 Small companies and groups are currently defined in section 247-249 of the Companies Act 1985. In broad terms, such entities are those which meet at least two of the following criteria: turnover not exceeding £2.8m, balance sheet total not exceeding £1.4m, no more than 50 employees. In its White Paper on "Modernising Company Law", the Government is proposing to increase the first two thresholds to the EU maximum of £4.8m and £2.4m respectively. To these small companies, the ASB offers the option of applying the FRSSE (Financial Reporting Standard for Smaller Entities). This essentially brings together in one place, with some simplification, the accounting requirements as they apply to small companies in each of the full standards. The IASB does not currently have a standard for smaller entities, although it has recently added the development of one to its workplan.

Relationship of the Regulation with other existing and proposed legislation

The existing EU Accounting Directives

3.12 For companies covered by the Regulation, adopted IAS will replace all the detailed accounting provisions of the Accounting Directives: that is to say, the 4th and 7th Directives on the annual and consolidated accounts of companies (Directives 78/660/EEC and 83/349/EEC respectively); the Directive on the annual and consolidated accounts of insurance undertakings (Directive 91/674/EEC); and the Directive on the annual and consolidated accounts of banks and other financial institutions (Directive 86/635/EEC). These provisions have been transposed into British legislation, mostly in schedules to the Companies Act 1985. The effect of the Regulation is that adopted IAS will be directly applicable and will have the force of law in each Member State. They will not require legislative action by the Member State to turn them into provisions of domestic law. In this country, they will directly supersede all the detailed accounting provisions of the Companies Act 1985 for the companies to which the Regulation applies. The IAS will not appear in our statute law.

3.13 The main parts of the Accounting Directives that will still apply to companies covered by the Regulation will be the general requirements to prepare the accounts and requirements relating to the audit, the directors' report and publication of accounts, together with some disclosures in the notes to the accounts.

Fair Value Directive

3.14 The Government expects to consult on proposals to implement the changes made to the Accounting Directives to allow fair value accounting for financial instruments early next year.

Modernisation of Accounting Directives

3.15 On 28 May 2002 the European Commission published a proposed Directive to modernise the Accounting Directives. Although the proposal does not currently cover Directive 86/635/EEC on banks and other financial institutions, we expect it to be extended. The general purpose of this proposal is to:

- remove all existing conflicts between the Accounting Directives and IASB standards;

- ensure that all optional accounting treatments currently available under IASB standards are available to EU companies which continue to have the Accounting Directives as the basis of their accounting legislation (ie those companies which do not prepare their accounts in accordance with the IAS Regulation); and

- update the fundamental structure of the Accounting Directives so that they provide a framework for financial reporting that is both consistent with modern practice and flexible enough to allow for future developments in IASB standards.

3.16 The proposed changes are designed to remove all inconsistencies between the Accounting Directives and IASB standards in existence at 1 May 2002. Negotiations between Member States and the Commission commenced on these proposals in June, in a Working Group of the European Council of Ministers. They are expected to be concluded by next spring.

Existing and proposed GB legislation

3.17 The important difference between the Regulation regime and the domestic regime is that companies subject to the Regulation will not be subject to the detailed accounting provisions of the Companies Act, whereas those subject to the domestic regime will be.

3.18 The Government will amend the Companies Act 1985 as appropriate to identify clearly all the reporting requirements on those companies not subject to the Regulation as well as the residual (non-accounting) requirements that will continue to apply to those companies that are subject to the Regulation.

3.19 This consultation is separate from the Company Law Review, the longer-term fundamental review of core company law. The first part of the Government's response to the Company Law Review's proposals was published in the "Modernising Company Law" White Paper in July 2002.

3.20 There is a close link between some of the proposals in the White Paper and decisions taken in the light of this consultation on any extension to the Regulation. In particular, sections 4 and 5 of the White Paper contain proposals for a new domestic regime that would change the status of existing accounting standards. Powers would be devolved to a body (building on the existing ASB) charged with making detailed domestic requirements with direct legal force on a range of accounting, reporting and other issues. As far as accounting requirements are concerned, this would enable the removal of existing overlaps between primary legislation (the accounting schedules to the Companies Act 1985) and domestic accounting standards.

3.21 Clearly, a revised domestic regime would not in any event apply to the consolidated accounts of publicly traded UK companies covered by the Regulation. At the same time, any extension of the application of the Regulation would further limit the scope of the proposed new domestic regime. If the Government decided, in light of this consultation, to extend the application of the Regulation significantly, it would need to look again at these aspects of the White Paper's proposals.

<u>Early application of the Regulation</u>

3.22 Some Member States (including Germany and Italy) have already allowed certain companies to prepare their consolidated accounts in accordance with IASB standards as an alternative to national standards. The Government has not intended allowing this here because there would be conflicts between the Accounting Directives and IASB standards. It would also means that companies in the same position would have a choice of reporting regimes in the run up to 2005. This could cause confusion for users of accounts and allow companies to avoid more stringent existing standards in certain circumstances.

3.23 Such an approach might have advantages for some companies. As they have to move to IAS anyway, it may suit them to do so sooner rather than later. However, companies that wanted to have this flexibility will still be subject to the detailed provisions of the Companies Act implementing the EU Accounting Directives until 2005. The Accounting Directives do not currently allow some companies to comply fully with IASB standards in several areas. Negotiations are currently in progress to remove these conflicts, but the necessary amending directive is unlikely to be in force before spring (see paragraphs 3.15 and 3.16). The changes, together with the amendments allowing fair value accounting for financial instruments (see paragraph 3.14), would then need to be implemented into British law. This would probably not be completed until at least late 2003 for the fair value amendments, and at least early 2004 for the modernisation amendments. Implementation of the Fair Value Directive alone would probably allow most companies to comply with virtually all existing IASB standards. But it seems highly unlikely that it would be possible for companies to comply fully with both the detailed provisions of the Accounting Directives and IASB standards until at least financial years commencing January 2004.

Implications for the tax regime

3.24 The profits shown by the annual accounts of individual companies have formed the base for taxing company profits for a long time. At present, only annual accounts drawn up under domestic accounting standards (also known in this context as UK generally accepted accounting principles or UK GAAP) are accepted as the base for corporation tax. If there is an extension to the application of the Regulation to individual accounts, the Government will want to consider the case for extending references to UK GAAP in tax legislation so as to include the application of relevant adopted IAS; and to review the impact that a change in particular accounting rules might have on the calculation of taxable profits.

LLPs and other undertakings

3.25 This consultation does not apply to LLPs, or to undertakings that are prudentially regulated under FSMA and do not have the status of companies. Such entities are not covered by the Regulation or its options. Voluntary or compulsory application of IAS to them would require different legislative means. This will need to be addressed once the Government has decided on the exercise of the Member State options.

Enforcement

3.26 The Regulation does not set out enforcement requirements. Instead, it will be for each Member State to put in place effective and proportionate measures. The European Commission is considering the development of EU and national mechanisms to ensure the proper and harmonised application of adopted IAS within the EU, in coordination with the Committee of European Securities Regulators. A report on enforcement principles from the Committee to the Commission is expected in September.

3.27 In Britain, there is already a well-regarded enforcement regime in place for ensuring that financial statements meet the requirements of existing legislation, including the requirement to give a true and fair view. Currently, the Financial Reporting Review Panel (FRRP) has legal authority to review companies' accounts and if necessary go to court to compel a company to revise its accounts. It shares this authority with the Secretary of State. By administrative agreement the FRRP deals with the accounts of large public and private companies, and the Secretary of State (through Companies House) with the rest. The Government's present intention is to retain this enforcement system for ensuring compliance with adopted IAS.

4. ANALYSIS OF THE OPTIONS

4.1 The following analysis is intended to assist consultees in reaching a view. It is not intended to reflect a Government view on the merits or otherwise of the options regarding extension of the application of the Regulation. The Government wishes to see the responses to the consultation before reaching a decision on the matter.

4.2 The Government does not believe there is a case for deferring application of the Regulation until 2007 for certain companies.

4.3 The following analysis considers first the case for any extension to the application of the Regulation, followed by the pros and cons of a voluntary or obligatory extension. It then goes on to look at the pros and cons of the options for extension. There are a large number of possible options for extension, but only the main ones are examined in this document. Finally, it considers the pros and cons of delaying application of the Regulation until 2007 in two specific cases.

Should the application of the Regulation be extended at all?

4.4 On the basis of its minimum requirement (application to the consolidated accounts of publicly traded companies) the Regulation will affect around 2700 UK companies. A general argument in favour of extension beyond that minimum can be made, particularly for any companies that do business or seek capital across borders. Compliance with adopted IAS would make their accounts more comparable with those of their competitors. This comparability would assist shareholders, analysts and other users of accounts and help to maintain the attractiveness of UK companies to international investors. There could also be cost savings as a result of not having to prepare different accounts according to different national standards.

4.5 Not extending the application of the Regulation, at least to some companies, could result in an artificial barrier to growth. For example, non-publicly traded companies to which the Regulation did not apply might be deterred from obtaining admission to trading on a regulated market by the need to change their past accounts to adopted IAS to provide the necessary historical three year record.

4.6 On the other hand, there will be cost implications in complying with the Regulation, for example, one-off conversion costs to the new system.

Any extension of the application of the Regulation would extend this burden, rather than confining it to the smallest possible number of companies and to those larger companies who are arguably best placed to cope.

4.7 In the light of the ASB's convergence programme, it is difficult to judge the scale of the potential disadvantages of extending or not extending the application of the Regulation. In the future, UK standards are likely to be very similar to IASB standards in many respects, but there will also be differences. In particular, ASB standards intended for use by non-publicly traded companies will sometimes regulate with a lighter touch than the equivalent IASB standards, which tend to focus on large publicly traded companies. They will, however, be based on the same principles as IASB standards, and will normally not prevent those that wish to do so from following any more detailed IASB standards where these comply with the Accounting Directives. It could be argued that if the degree of convergence was high, the application of the Regulation could be extended with little extra cost or potential confusion, whereas if the degree of convergence was low, the cost of extension would be higher.

4.8 There is also an argument that by extending the application of the Regulation so that fewer (and possibly only the smaller) companies comply with domestic standards, the UK's influence in the development of IASB standards, currently led by the ASB, may over time be weakened. Such concerns may need to be taken into account when deciding whether to extend the application of the Regulation.

4.9 If the application of the Regulation is extended to the individual accounts of any companies, changes may need to be made to tax legislation (see paragraph 3.24).

4.10 It is worth bearing in mind that any extension to the application of the Regulation would not necessarily need to be implemented by 2005.

1. Should the Government extend the application of the Regulation, beyond the requirement for the consolidated accounts of publicly traded companies to comply with adopted IAS? Please give reasons for your view.

<u>Voluntary versus obligatory extension of the Regulation</u>

4.11 At first sight, a voluntary regime would appear to have a number of advantages. The Government would simply allow each individual company to which the option of using adopted IAS was extended to choose for itself whether or not to use IAS. Companies that so chose would be able to prepare accounts in accordance with adopted IAS. Companies that chose not to use adopted IAS (and any to which the option of using IAS was not extended) would continue to comply with the domestic accounting regime.

4.12 However, in practice the extent of freedom of choice for any particular company will depend on the extent to which domestic accounting standards differ from adopted IAS. As indicated above, the ASB's convergence programme may establish a situation where UK companies will have to comply with domestic accounting standards that are often similar to adopted IAS. If convergence eventually approaches 100%, it is arguable that all UK companies will by then be subject to IAS one way or another, regardless of whether the application of the Regulation is extended. There would then be little difference in practice (or in compliance costs) between obligatory or voluntary application of adopted IAS under the Regulation. However, if there were significant differences between the two sets of standards, as may occur if the ASB simplifies certain IASB standards for non-publicly traded companies, there would be greater practical differences between obligatory or voluntary application.

4.13 On the other hand, a voluntary regime would also have a number of disadvantages: the greater any divergence between domestic accounting standards and adopted IAS, the greater these disadvantages would be. The use of two different regimes (even if different in only minor ways) would lead to a loss of comparability between companies within UK, especially those of the same size in the same sector. Also, companies may choose an accounting regime that flatters their own particular situation. As a result, investors, creditors and other users of accounts could be disadvantaged. Enforcement would be more complicated, because the authorities would have to acquire and retain expertise in two sets of standards and in whether compliance provided a true and fair view. Technical complications would arise. Having opted into adopted IAS, could a company subsequently opt out? For how long a period would it have to use adopted IAS? How would it take the decision to opt in or out? All these questions would probably require additional legislation.

4.14 As for the merits of an obligatory regime, if adopted IAS are very similar to UK accounting standards, the obligatory approach carries no additional costs and adds legal certainty as well as authority. If adopted IAS and UK accounting standards are divergent, the obligatory approach avoids confusion.

2. If you think that the Regulation should be extended, do you consider that this should be:

(a) on a voluntary basis whereby the Government permits some or all companies to comply with adopted IAS?

(b) on a compulsory basis whereby the Government requires some or all companies to comply with adopted IAS?

Please give reasons for your view.

<u>If the application of the Regulation were to be extended, how far should it be extended?</u>

Option (i): Extension of the application of the Regulation to the individual accounts of publicly traded companies

4.15 There may be good reasons to exercise this option in order to help internal consistency and comparability of accounts within the same group and assist in preparation of consolidated accounts. There is the additional advantage that the current practice of presenting entity financial statements of the parent with the group accounts as one package could continue. With no extension the practice would probably have to change, as it would be cumbersome and confusing to have to explain two different bases of preparation. We estimate that this would affect around 2700 companies.

Option (ii) - Option (i) plus extension of the application of the Regulation to the individual accounts of subsidiaries of publicly traded companies

4.16 There may also be good reasons for adopting this option. It would be easier and cheaper for subsidiaries to prepare their accounts in the same way as their parent company. If subsidiaries were not allowed to use adopted IAS, they would have to prepare two sets of accounts: one using UK accounting standards for themselves, and one using IAS for their parent company for consolidation purposes. This would increase complexity and cost. It is difficult to say how many companies this would affect; if each parent company had an average of 10 active subsidiaries, it would affect around an additional 27,000 companies.

Option (iii) – Extension of the application of the Regulation to the individual accounts of publicly traded companies that do not produce consolidated accounts.

4.17 The most prominent of these are likely to be investment companies, in particular investment trusts. Such companies tend not to produce consolidated accounts, either because they do not have subsidiaries or because their subsidiaries may not be consolidated for various reasons. As the Regulation applies to all other publicly traded companies, it would seem sensible also to extend it to this category of publicly traded companies, to avoid having a dual system of reporting at the publicly traded level.

4.18 Investment trust companies are usually investment companies as defined in section 266 of the Companies Act 1985 and are therefore subject to special conditions relating to distributions of income receivable from securities. If a decision was made to extend the application of the Regulation to investment companies, then in view of the move to fair value accounting (in particular for financial instruments and the probable impact on their "income"), a change to the definition of investment companies in the Companies Act 1985 may need consideration.

4.19 We estimate that this would affect around 250 companies.

Option (iv) - Options (i) to (iii) plus extension of the application of the Regulation to large and medium sized non-publicly traded companies (all companies above those small companies that could apply the ASB's FRSSE)

4.20 A case can also be made for extending the Regulation to large and medium sized non-publicly traded companies. Larger companies are most likely to be compared with competitors that are publicly traded and to seek admission to trading on a regulated market in the future. Extending the application of the Regulation would make it easier for them to apply for admission. Such companies are normally required to give a three year history in their prospectus. It would be costly and time consuming to restate the UK accounts to adopted IAS.

4.21 On the other hand, IASB standards are developed with large publicly traded companies in mind, and may not be entirely suitable for non-publicly traded companies in all cases. Therefore, the burden of using adopted IAS is likely to be greater for non-publicly traded companies than for public traded companies, in terms of complexity and having to work out which standards or parts of standards are relevant to them.

4.22 The greater the degree of convergence between adopted IAS and UK accounting standards as they relate to non-publicly traded companies, the stronger the case for extending the application of the Regulation to all companies larger than those small companies who could apply the ASB's FRSSE, since they will already in effect be complying with adopted IAS.

4.23 We estimate that this could affect around 70,000 to 80,000 active companies.

Option (v) - Extension of the application of the Regulation to all companies, including those that could apply the ASB's FRSSE.

4.24 At first sight, this option would appear to impose a significant burden on small companies. IASB standards are primarily focused on the reporting requirements of large publicly traded companies that are involved in complex transactions. Some standards are irrelevant to small companies as they deal with transactions that small companies do not conduct, or require small companies to account for certain transactions in overly complex ways (for example IAS39 on financial instruments). The same is true, to a lesser extent, of ASB standards. However, to help small companies in the UK, the ASB developed the FRSSE, which brings together in one place, with some simplifications, the accounting requirements from each of the full domestic standards as they apply to small companies. The IASB has only recently added the development of an international standard for small entities to its workplan. Until an international standard for small entities is developed, applying full adopted IAS to small companies could present a significant burden to them or their accountants, in terms of having to work out which parts of adopted IAS are relevant to them, and in some cases complying with extensive requirements.

4.25 On the other hand, depending on the degree of convergence of domestic and international standards, and the possible development of an international standard for small entities, the application of adopted IAS to even the smallest companies may be less burdensome than it first appears. The benefit would be a single regime of accounting standards within the UK, with all that entails in terms of comparability and clarity, as well as equality in terms of enforcement. By contrast, operating two different accounting regimes for companies of whatever size within the same industrial sectors would be likely to generate confusion and have the disadvantages referred to in paragraph 4.13.

4.26 If there was a demand for the application of the Regulation to be extended to the smallest companies, it may be that some sort of transitional arrangement for a domestic FRSSE based on adopted IAS could be put in place by the ASB until an appropriate international standard was available.

4.27 Extension of the application of the Regulation to all companies would affect some 1.3m active companies, including over 1.2m active small companies.

Option (vi) – Possible sector-specific extension of the application of the Regulation

4.28 It may be sensible to consider extending the application of the Regulation to publicly traded companies that do not produce consolidated accounts and non-publicly traded companies that are prudentially regulated under FSMA, regardless of whether any other extensions are made. Regulation of the sector would be facilitated if the accounts of publicly traded and non-publicly traded companies were prepared on a consistent basis. It is difficult to estimate how may companies would be affected.

3. If you think that the Regulation should be extended, to which accounts and companies do you think the extension should apply?

(i) the individual accounts of publicly traded companies?

(ii) the individual accounts of the subsidiaries of publicly traded companies?

(iii) the individual accounts of publicly traded companies that do not produce consolidated accounts?

(iv) the individual and/or consolidated accounts of large and medium sized publicly traded companies, eg all companies above those small companies that could apply the ASB's FRSSE?

(v) the individual and/or consolidated accounts of all companies?

(vi) the individual and/or consolidated accounts of all companies that are prudentially regulated under FSMA?

Please give reasons for your view.

Deferring application of the Regulation until 2007

4.29 Application of the Regulation can be deferred until financial years starting on or after 1 January 2007 for:

- Companies that only have debt securities admitted to trading on a regulated market of any Member State; and

- Companies whose securities are admitted to trading in a non EU country and for that purpose have been using internationally accepted standards since the financial year that started prior to the date of publication of the Regulation. (Recital (17) to the Regulation states that the standards must be used as the primary basis for preparing consolidated accounts. Therefore, the vast majority of UK companies that have securities traded on non EU markets, for example those that prepare a reconciliation to US GAAP, would not be eligible for deferral).

4.30 There are just over 500 companies that only have debt securities traded. A sound argument can be made for saying that the ASB's standards are "internationally accepted", but we believe that less than 20 UK companies have securities traded on non EU markets without a reconciliation to another GAAP.

4.31 Deferral until 2007 may have advantages for some companies and their advisers, in particular giving them more time to prepare for using adopted IAS. However, using reporting standards that may differ from adopted IAS for an additional two years may create difficulties for the small minority of companies potentially affected, in that investors and others are likely to expect and want all publicly traded companies in the EU to be using the same accounting standards for their consolidated accounts.

4.32 In view of the comparatively small number of companies potentially affected, and the difficulties for all concerned of having two separate reporting regimes for companies covered by the Regulation between 2005 and 2007, there does not seem to be any justification for deferring the application of the Regulation in these cases. However, views are invited from consultees before a final decision is taken.

4. Do you consider that the application of the Regulation should be deferred until 1 January 2007 for:

(a) publicly traded companies that have only their debt securities (eg bonds) admitted on a regulated market in the EU?

(b) publicly traded companies whose securities are admitted to trading on markets outside the EU and which use internationally accepted accounting standards?

Please give reasons for your view.

Cost implications

4.33 The attached draft Regulatory Impact Assessment (Annex D) seeks comments on the likely costs and benefits of the various options for extending the application of the Regulation, and of not doing so. It indicates where costs and benefits are likely to occur and offers initial estimates for these. It would be very helpful if consultees could comment on the potential costs and benefits, for their company or more generally, of any or all of the options. Information on additional costs and benefits would also be welcomed.

5. Can you:

(a) identify any costs or savings for your company or more generally resulting from the above options for extension or delay of the Regulation and hence the application of adopted IAS?

(b) quantify those costs or savings?

You may wish say what impact the ASB's ongoing convergence programme (designed to bring UK accounting standards into line with IASB standards) might have on these costs or savings.

LLPs and other undertakings

4.34 As the Regulation does not apply to LLPs, voluntary or compulsory application of the IAS Regulation would require the use of powers in the LLP Act. This will need to be addressed once the Government has decided on the exercise of the Member State options. The Government's general policy on LLPs is to treat them in the same way as companies of the same size unless this is clearly inappropriate.

4.35 Similarly, the consultation does not apply directly to undertakings that are prudentially regulated under FSMA and do not have the status of companies. Again, the Government's general policy on these undertakings is to treat them in the same way as companies of the same size and sector.

4.36 The Government is taking advantage of the consultation to inform any consequential decisions relating to LLPs and other undertakings.

6. Should LLPs, and undertakings that are prudentially regulated under FSMA and do not have the status of companies, also be permitted or required to prepare their accounts in accordance with adopted IAS, on the same basis as companies of the same size and sector? (Note that this could not be done as part of this exercise, but would have to be done separately.)

Please give reasons for your view.

Annex A

REGULATION (EC) No /2002 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on the application of international accounting standards

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

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

Having regard to the proposal from the Commission [1],

Having regard to the opinion of the Economic and Social Committee [2]

Acting in accordance with the procedure laid down in Article 251 of the Treaty [3],

[1] OJ C 154 E, 29.5.2001, p. 285.
[2] OJ C 260, 17.9.2001, p. 86.
[3] Opinion of the European Parliament of 12 March 2002 (OJ C) and Decision of the Council of .

Whereas:

(1) The Lisbon European Council of 23-24 March 2000 emphasised the need to accelerate completion of the internal market for financial services, set the deadline of 2005 to implement the Commission's Financial Services Action Plan and urged that steps be taken to enhance the comparability of financial statements prepared by publicly traded companies.

(2) In order to contribute to a better functioning of the internal market, publicly traded companies must be required to apply a single set of high quality international accounting standards for the preparation of their consolidated financial statements. Furthermore, it is important that the financial reporting standards applied by Community companies participating in financial markets are accepted internationally and are truly global standards. This implies an increasing convergence of accounting standards currently used internationally with the ultimate objective of achieving a single set of global accounting standards.

(3) Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies [4], Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts [5], Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions [6] and Council Directive 91/674/EEC on the annual accounts and consolidated accounts of insurance companies [7] are also addressed to publicly traded Community companies. The reporting requirements set out in these Directives cannot ensure the high level of transparency and comparability of financial reporting from all publicly traded Community companies which is a necessary condition for building an integrated capital market which operates effectively, smoothly and efficiently. It is therefore necessary to supplement the legal framework applicable to publicly traded companies.

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[4] OJ L 222, 14.8.1978, p.11. Directive as last amended by European Parliament and Council Directive 2001/65/EC (OJ L 283, 27.10.2001, p. 28).
[5] OJ L 193, 18.7.1983, p. 1. Directive as last amended by European Parliament and Council Directive 2001/65/EC.
[6] OJ L 372, 31.12.1986, p. 1. Directive as last amended by European Parliament and Council Directive 2001/65/EC.
[7] OJ L 374, 31.12.1991, p. 7.

(4) This Regulation aims at contributing to the efficient and cost-effective functioning of the capital market. The protection of investors and the maintenance of confidence in the financial markets is also an important aspect of the completion of the internal market in this area. This Regulation reinforces the freedom of movement of capital in the internal market and helps to enable Community companies to compete on an equal footing for financial resources available in the Community capital markets, as well as in world capital markets.

(5) It is important for the competitiveness of Community capital markets to achieve convergence of the standards used in Europe for preparing financial statements, with international accounting standards that can be used globally, for cross-border transactions or listing anywhere in the world.

(6) On 13 June 2000, the Commission published its Communication on "EU Financial Reporting Strategy: the way forward" in which it was proposed that all publicly traded Community companies prepare their consolidated financial statements in accordance with one single set of accounting standards, namely International Accounting Standards (IAS), at the latest by 2005.

(7) International Accounting Standards (IASs) are developed by the International Accounting Standards Committee (IASC), whose purpose is to develop a single set of global accounting standards. Further to the restructuring of the IASC, the new Board on 1 April 2001, as one of its first decisions, renamed the IASC as the International Accounting Standards Board (IASB) and, as far as future international accounting standards are concerned, renamed IAS as International Financial Reporting Standards (IFRS). These standards should, wherever possible and provided that they ensure a high degree of transparency and comparability for financial reporting in the Community, be made obligatory for use by all publicly traded Community companies.

(8) The measures necessary for the implementation of this Regulation should be adopted in accordance with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission [8] and with due regard to the declaration made by the Commission in the European

[8] OJ L 184, 17.7.1999, p. 23.

Parliament on 5 February 2002 concerning the implementation of financial services legislation.

(9) To adopt an international accounting standard for application in the Community, it is necessary firstly that it meets the basic requirement of the aforementioned Council Directives, that is to say that its application results in a true and fair view of the financial position and performance of an enterprise - this principle being considered in the light of the said Council Directives without implying a strict conformity with each and every provision of those Directives; secondly that, in accordance with the conclusions of the Council of 17 July 2000, it is conducive to the European public good and lastly that it meets basic criteria as to the quality of information required for financial statements to be useful to users.

(10) An accounting technical committee should provide support and expertise to the Commission in the assessment of international accounting standards.

(11) The endorsement mechanism should act expeditiously on proposed international accounting standards and also be a means to deliberate, reflect and exchange information on international accounting standards among the main parties concerned, in particular national accounting standard setters, supervisors in the fields of securities, banking and insurance, central banks including the ECB, the accounting profession and users and preparers of accounts. The mechanism should be a means to foster common understanding of adopted international accounting standards in the Community.

(12) In accordance with the principle of proportionality, the measures provided for in this Regulation, in requiring that a single set of international accounting standards be applied to publicly traded companies, are necessary to achieve the objective of contributing to the efficient and cost-effective functioning of Community capital markets and thereby to the completion of the internal market.

(13) In accordance with the same principle, it is necessary, as regards annual accounts, to leave to Member States the option to permit or require publicly traded companies to prepare them in conformity with international accounting standards adopted in accordance with the procedure laid down in this Regulation. Member States may decide as well to extend this permission or this requirement to other companies

as regards the preparation of their consolidated accounts and/or their annual accounts.

(14) In order to facilitate an exchange of views and to allow Member States to coordinate their positions, the Commission should periodically inform the accounting regulatory committee about active projects, discussion papers, point outlines and exposure drafts issued by the IASB and about the consequential technical work of the accounting technical committee. It is also important that the accounting regulatory committee is informed at an early stage if the Commission intends not to propose to adopt an international accounting standard.

(15) In its deliberations on and in elaborating positions to be taken on documents and papers issued by the IASB in the process of developing international accounting standards (IFRS and SIC-IFRIC), the Commission should take into account the importance of avoiding competitive disadvantages for European companies operating in the global marketplace, and, to the maximum possible extent, the views expressed by the delegations in the Accounting Regulatory Committee. The Commission will be represented in constituent bodies of the IASB.

(16) A proper and rigorous enforcement regime is key to underpinning investors' confidence in financial markets. Member States, by virtue of Article 10 of the Treaty, are required to take appropriate measures to ensure compliance with international accounting standards. The Commission intends to liaise with Member States, notably through the Committee of European Securities Regulators (CESR), to develop a common approach to enforcement.

(17) Further, it is necessary to allow Member States to defer the application of certain provisions until 2007 for those companies publicly traded both in the Community and on a regulated third-country market which are already applying another set of internationally accepted standards as the primary basis for their consolidated accounts as well as for companies which have only publicly traded debt securities. It is nonetheless crucial that by 2007 at the latest a single set of global international accounting standards, the IAS, apply to all Community companies publicly traded on a Community regulated market.

(18) In order to allow Member States and companies to carry out the necessary adaptations to make the application of international

accounting standards possible, it is necessary to apply certain provisions only in 2005. Appropriate provisions should be put in place for the first-time application of IAS by companies as a result of the entry into force of the present regulation. Such provisions should be drawn up at international level in order to ensure international recognition of the solutions adopted,

HAVE ADOPTED THIS REGULATION:

Article 1

Aim

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

Article 2

Definitions

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

Article 3

Adoption and use of international accounting standards

1. In accordance with the procedure laid down in Article 6(2), the Commission shall decide on the applicability within the Community of international accounting standards.

2. The international accounting standards can only be adopted if:

- they are not contrary to the principle set out in Article 2(3) of Directive 78/660/EEC and in Article 16(3) of Directive 83/349/EEC and are conducive to the European public good and,

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

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

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

Article 4

Consolidated accounts of publicly traded companies

For each financial year starting on or after 1 January 2005, companies governed by the law of a Member State shall prepare their consolidated accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) if, at their balance sheet date, their securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field.[9]

Article 5

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

Member States may permit or require

(a) the companies referred to in Article 4 to prepare their annual accounts,

[9] OJ L 141, 11.6.1993, p. 27. Directive as last amended by European Parliament and Council Directive 2000/64/EC (OJ L 290, 17 .11.2000, p. 27).

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

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

Article 6

Committee Procedure

1. The Commission shall be assisted by an accounting regulatory committee hereinafter referred to as "the Committee".

2. Where reference is made to this paragraph, Articles 5 and 7 of Decision 1999/468/EC shall apply, having regard to the provisions of Article 8 thereof.

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

3. The Committee shall adopt its rules of procedure.

Article 7

Reporting and coordination

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

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

Article 8

Notification

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

Article 9

Transitional provisions

By way of derogation from Article 4, Member States may provide that the requirements of Article 4 shall only apply for each financial year starting on or after January 2007 to those companies:

(a) whose debt securities only are admitted on a regulated market of any Member State within the meaning of Article 1(13) of Directive 93/22/EEC; or

(b) whose securities are admitted to public trading in a non-member state and which, for that purpose, have been using internationally accepted standards since a financial year that started prior to the publication of this Regulation in the Official Journal of the European Communities.

Article 10

Information and Review

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

Article 11

Entry into force

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

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

Done at Brussels,

For the European Parliament	For the Council
The President	The President

ANNEX B

EXPLANATORY NOTE TO THE REGULATION

(This note has been produced by the Department of Trade and Industry and is not part of the Regulation)

Preamble

1. While the preamble and its recitals (1) - (18) do not form part of the legislation itself, they may be used by a court in interpreting the purpose and effect of the Regulation. The preamble describes the background to and rationale for the Regulation and how it is intended to work, including the procedure for endorsement of international accounting standards by the Member States and the Commission.

Article 1: Aim

2. The aim is to harmonise the financial information disclosed by the companies covered by the Regulation, thus enhancing their transparency and comparability and improving the operation of the Community's capital market and internal market.

Article 2: Definitions

3. Under the Regulation, "international accounting standards" means accounting standards and related interpretations issued by the IASB prior to and following the Regulation's adoption.

Article 3: Adoption and use of international accounting standards

4. The Commission will only adopt an IAS if it meets certain criteria set out in this article (see paragraphs 7 - 11 for the procedure on the adoption of IAS). By 31 December 2002, the Commission must decide whether to adopt IASB standards in existence as of the date of entry into force of Regulation. As of the date of publication of this consultation document, the Regulation has not yet been published in the Official Journal. It will enter into force three days after publication in the Official Journal. All adopted IAS are to be translated into the official languages of the Community and published in the Official Journal.

Article 4: Consolidated accounts of publicly traded companies

5. For each financial year starting on or after 1 January 2005, the Regulation applies to the consolidated accounts of publicly traded companies.

Article 5: Options in respect of annual accounts and of non-publicly traded companies

6. This Article gives Member States the options described earlier of extending (through a voluntary or obligatory system) the application of the Regulation and hence compliance with adopted IAS.

Articles 6 and 7: Committee Procedure & Reporting and Coordination

7. These articles deal with the procedure by which IAS will be adopted. The Regulation establishes an “Accounting Regulatory Committee” (ARC), which will decide, with the Commission, on the adoption of IASB standards. The ARC consists of official representatives from Member States and is chaired by the Commission. It met informally for the first time on 17 July and is due to meet again on 24 September.

8. A technical committee of experts will advise the European Commission on the suitability of IAS. The Commission has made arrangements with the European Financial Reporting Advisory Group (EFRAG), comprising independent accounting experts from the private sector, to fulfil that role.

9. Following advice from EFRAG, the Commission will be expected, in all but exceptional circumstances, to propose the adoption of the IAS in question to the ARC. The ARC will then vote on adoption of the IAS. The standard must be adopted in full or not at all. It cannot be amended by the Commission, the ARC or individual Member States. The decision will be based on qualified majority voting. If a qualified majority of the ARC are not in favour of adopting the standard, the Commission will submit the proposal to the Council of Ministers. The Council will then have a maximum of three months to adopt or block the proposal by qualified majority voting. If the Council blocks the proposal, the Commission may re-submit it. If the Council does not take any action, the Commission will apply the proposal.

10. The European Parliament also has the right to comment on the proposal, but it has no right of veto.

11. The Commission must keep the ARC informed of developments on IASB projects and obtain Member States' views on IASB proposals. If the Commission considers it will be unable to propose adoption of an IAS, it must report to the ARC in a timely manner.

Article 8: Notification

12. If a Member State exercises any of the options in Article 5 it must inform the Commission and the other Member States.

Article 9: Transitional provisions

13. This Article provides the option for Member States to defer application of the Regulation until January 2007 in two specific cases.

Article 10: Information and review

14. This Article requires the Commission to review the Regulation's operation and report to the Council by 1 July 2007.

Article 11: Entry into force

15. This provides for the date of the Regulation's entry into force and makes it binding and directly applicable in all Member States.

ANNEX C

List of the Regulated Markets Notified to the Commission by the Member States under Article 16 of the *ISD* as at 22 March 2001

Austria

1 Amtlicher Handel (official market)
2 Geregelter Freiverkehr (semi-official market)
3 Amtlicher Handel NEWEX (official market)
4 Geregelter Freiverkehr NEWEX (semi-official market)

Belgium

1 Bourse de valeurs mobilières d'Euronext Brussels:
- Le premier marché (official market)
- Le second marché
- Le nouveau marché

2 Belfox (Bourse belge des futures et options)
3 Le marché secondaire hors bourse des obligations linéaires, des titres scindés et des certificats de trésorerie
4 EASDAQ

Denmark

1 Københavns Fondsbørs
- Equity market
- Bond market
- Derivatives market

2 Dansk Autoriseret Markedsplads A/S (Danish Authorised Market Place Ltd. (DAMP) [authorised market place = regular trade in securities admitted for trading but not listed on stock exchange]

Finland

1 Arvopaperipörssi (Stock Exchange)
- Päälista (Main list for equity and Debt Instruments)
- I-, NM – ja Prelista (parallel Lists I-, NM-and pre-list for equity and debt instruments)

2 Optioyhteisö (Option Corporation)
(Derivatives exchange and clearing house)

France

1 Bourse de Paris:
- Premier marché (official list)
- Second marché
- Marché des EDR (European Depositary Receipts).

2 Nouveau marché
3 MATIF
4 MONEP

Germany

1 Berliner Wertpapierbörse: (Amtlicher Handel, Geregelter Markt)
2 Bremer Wertpapierbörse (Amtlicher Handel, Geregelter Markt)
3 Rheinisch-Westfälische Börse zu Düsseldorf (Amtlicher Handel, Geregelter Markt)
4 Frankfurter Wertpapierbörse (Amtlicher Handel, Geregelter Markt, Neuer Markt)
5 Eurex Deutschland
6 Hanseatische Wertpapierbörse Hamburg (Amtlicher Handel, Geregelter Markt, Start-up market)
7 Niedersächsische Börse zu Hannover (Amtlicher Handel, Geregelter Markt)
8 Bayerische Börse (Amtlicher Handel, Geregelter Markt)
9 Baden-Württembergische Wertpapierbörse (Amtlicher Handel, Geregelter Markt)

Greece

1 Athens Stock Exchange (A. S. E.)/Thessaloniki Stock Exchange Centre (T. S. E. C. = remote platform)
- Main Market
- Parallel Market
- Parallel Market for Emerging Markets
- New Market

2 Athens Derivatives Exchange (A. D. EX.)

Ireland

Irish Stock Exchange comprising:
- Official List
- Exploration Securities Market
- Developing Companies Market
- ITEQ

Italy

1 Stock Exchange, divided into the following segments:
- Electronic share market (MTA)
- Electronic covered warrants market (MCW)
- After-Hours Market (TAH)
- Electronic bond and government securities market (MOT)
- Electronic market for Eurobonds, foreign bonds and asset-backed securities (EuroMOT)
- Electronic traditional options market (MPR)

2 Mercato Ristretto (second market)
3 Derivatives market (IDEM)
4 Nuovo Mercato (New Market – NM)
5 Italian Government Securities Derivatives Market (MIF)
6 Wholesale Market for Government Securities (MTS)
7 Wholesale Market for Corporate and International Organisations Bonds.

Luxembourg

Bourse de Luxembourg:
- Main market
- International Bond market

Netherlands

Amsterdam Stock Exchange (AEX)
- Main market
- Domestic market for unlisted secutiries
- Nieuwe Markt Amsterdam

Portugal

1 Mercado de Cotações Oficias (Official Quotation Market)
2 Segundo Mercado (Second Market)
3 Novo Mercado (New Market)
4 Mercado de Futuros e Opções (Futures and Options Market)
5 MEOG – Mercado Especial de Operações por Grosso (Special Market for Block Trading)
6 MEDIP – Mercado Especial de Dívida Pública (Special Market for Public Debt)

Spain

A. Bolsas de Valores (all comprise first, second and new market segments)
1 Bolsa de Valores de Barcelona
2 Bolsa de Valores de Bilbao
3 Bolsa de Valores de Madrid
4 Bolsa de Valores de Valencia
B. Mercados oficiales de Productos Finacieros Derivados
1 MEFF Renta Fija
2 MEFF Renta Variable
C. Mercados FC&M de Futuros y Opciones sobre Cítricos [commodity derivatives not covered by section B annex ISD: related markets do not fall within ISD definition of "regulated market"]

D. AIAF Mercado de Renta Fija

E. Mercado de Deuda Pública en Anotaciones

Sweden

1 OM Stockholmbörsen
- "A-list" market
- "OTC – list" (small companies)
- "O-list" (unlisted companies)

2 OM Räntebörsen (fixed income)
3 SBI Marknadsplats
4 Aktietorget

United Kingdom

1 Domestic Equity Market
2 European Equity Market
3 Gilt Edged and Sterling Bond Market
4 Alternative Investment Market (AIM).
5 The London International Financial Futures and Options Exchange (LIFFE)
6 OM London
7 Tradepoint [this market has since changed its name to virt-x]
8 Coredeal (primarily a eurobond market)
9 Jiway

List of the regulated markets notified under Article 16 of the ISD, as included in point 30b of Annex IX to the Agreement of the European Economic Area, to the Standing Committee of the EFTA as defined in that agreement as at April 2001

Iceland

Iceland Stock Exchange (Verdbrefathing Islands)
Iceland OTC market

Liechtenstein

Norway

The Oslo Stock Exchange

ANNEX D

DRAFT REGULATORY IMPACT ASSESSMENT

INTERNATIONAL ACCOUNTING STANDARDS REGULATION – EXERCISE OF MEMBER STATE OPTIONS

Issue

1. The Regulation of the European Parliament and of the Council on the Application of International Accounting Standards was adopted by Member States on 7 June 2002. It requires companies governed by the law of a Member State whose securities are admitted to trading on a regulated market in any Member State in the EU ("publicly traded companies") to prepare their consolidated accounts on the basis of International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB), from 1 January 2005.

2. The Regulation contains options allowing Member States to permit or require:

- publicly traded companies to prepare their individual accounts in accordance with adopted IAS;

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

3. The Regulation also gives Member States the option to defer application of the Regulation until January 2007 for companies who have only their debt securities (eg bonds) publicly traded on a regulated market, or who are publicly traded on markets outside the EU and currently use internationally accepted accounting standards.

Purpose

4. The purpose of the Regulation is to increase comparability, consistency and transparency of accounts across Member States and worldwide. We now need to consider the advantages and disadvantages of extending the application of the Regulation.

Effect

5. For publicly traded companies, adherence to adopted IAS should help reduce the cost of capital because their accounts will be more accessible to potential investors across the EU and worldwide. For potential investors, creditors and other users of financial statements, adopted IAS provide a single measure by which to compare performance and prospects on a like-for-like basis.

6. For those UK companies affected, the Regulation will have 2 main impacts: they will have to comply with accounting standards drawn up by the IASB, as distinct from the domestic accounting standards issued by the Accounting Standards Board (ASB); and those standards will have direct legal force.

7. In the UK, the ASB's accounting standards apply to all companies. ASB and IASB standards are in many cases very similar, although there are also a number of differences. The ASB is concentrating its effects on achieving convergence between UK accounting standards and IASB's standards, but differences will remain. Depending on the degree of comparability between UK accounting standards and adopted IAS, some companies may, in effect, be preparing their accounts in accordance with adopted IAS regardless of whether the Regulation is extended.

Risks

8. Not extending the application of the Regulation, at least to some companies, could result in an artificial barrier to growth. For example, non-publicly traded companies to which the Regulation did not apply might be deterred from obtaining admission to trading on a regulated market by the need to change their past accounts to adopted IAS to provide the necessary three year record.

9. On the other hand there will be cost implications in complying with the Regulation, for example, one-off convention costs to the new system. Any extension of the application of the Regulation would extend the burden, rather than confining it to the smallest possible number of companies and to those larger companies who are arguably best placed to cope.

Identify Options

10. There are many options for extending the application of the Regulation, from no extension, through extension to certain types, sizes, or business sectors of company, to full extension to all companies.

11. The main options are listed below:

Option 1:	No extension to the application of the Regulation.
Option 2(i):	Extension of the application of the Regulation to the individual accounts of publicly traded companies.
Option 2(ii):	Option 2(i) plus extension of the application of the regulation to the individual accounts of subsidiaries of publicly traded companies.
Option 2(iii):	Extension of the application of the Regulation to the individual accounts of publicly traded companies that do not produce consolidated accounts.
Option 2(iv):	Options 2(i) to 2(iii) plus extension of the application of the Regulation to large and medium-sized non-publicly trade companies (all companies above those small companies that could apply the ASB's FRSSE).
Option 2(v):	Extension of the application of the Regulation to all companies.
Option 2(vi):	Sector specific option: Extension of the application of the Regulation to companies prudentially regulated under the Financial Services and Markets Act 2000.

12. We expect Option 2(iii) to affect only medium to large companies. Option 2(vi) is the most likely option for a sector specific extension of the application. It could be a stand alone option or in addition to any of the other options discussed. We would not expect option 2(vi) to affect small companies.

Preferred Option

13. The Government does not have a preferred option and will make a decision after assessing the responses to the consultation.

Costs and Benefits of Options

14. The following paragraphs discuss the costs and benefits of extending or not extending the application of the Regulation. They indicate the areas where costs and benefits are most likely to occur, and give an initial estimate of the costs and benefits.

15. It would be very helpful if consultees could specify their preferred option and comment on the likely costs and benefits, both in terms of where these are likely to fall and the estimated amounts either for their company or more generally. Comments on the costs and benefits associated with any other options would also be very welcome. <u>It is important to note that the cost estimates within this RIA are initial estimates, and that these initial estimates will be revised following this consultation, in light of information provided by consultees.</u>

16. If consultees think there are likely to be other costs and benefits, information on these would be welcome.

17. As the Regulation has already been adopted, this RIA considers only the costs benefits of <u>extending</u> the application of the Regulation.

<u>Option 1</u>

18. If the application of the Regulation is not extended, there will be no cost to businesses other than that falling on companies already covered by the Regulation. This is taken as the base cost from which all other options are calculated. Any cost on shareholders, analysts and other users of accounts (such as investors, creditors and enforcement bodies) of having to be familiar with two sets of accounting regimes for investment or compliance purposes arises from the Regulation itself rather than any extension to it.

<u>Option 2(i) & 2(ii)</u>

19. The cost of extending the application of the Regulation to the individual accounts of publicly traded companies and the individual accounts of subsidiaries should be minimal. These companies would need to prepare

accounts to adopted IAS in order for the parent company to consolidate them into the group accounts already covered by the Regulation.

20. A benefit of this option is that the companies would not have to prepare their accounts using two accounting methods. Both individual accounts and account consolidations would be prepared to adopted IAS. We would estimate the time spent interrogating data in order to compile accounts to a particular accounting regime to be in the region of 2 people for between 4 and 10 days. Assuming cost of staff time to be approximately £100 per day (approximately £25,000 per annum) the cost savings for subsidiaries may be between £800 and £2000 per company per year (or between £21.6m (2 x £100 x 4 x 27,000) and £54m (2 x £100 x 10 x 27,000) for the sector as a whole). The cost savings for the parent companies would be £2000 per company per year (or £5.4m (2 x £100 x 10 x 2700) for the sector as a whole).

<u>Option 2(iii), 2(iv), 2(v) & Option 2(vi)</u>

21. The extension of the application of the Regulation to companies beyond parent companies and their subsidiaries already affected would have cost implications.

22. There will be a one-off cost in complying with the Regulation. Companies will have to change the basis on which they prepare their accounts, entailing changes to accounting systems. Changes to IT systems would be required, but we do not currently have estimates for these.

23. There will be one-off training costs for staff in being instructed in the standards and in interrogating the data in order to compile accounts to a particular accounting regime. Anecdotal evidence suggests that small companies may require 1 person to be trained for 2 days. Medium to large companies may require 2 staff to be trained for between 3 and 5 days. This gives the following estimates:

Cost of training course	£499 per day (cost of a one day training package on IAS)
Cost of staff time per day	£100 per day (assuming staff pay of £25,000 per annum approximately)

24. We estimate the training costs for small companies may be approximately £1200 per company (or £1,440m ((£499 x 2 + £100 x 2) x

1.2m) for the sector as a whole). It is possible that as many as 60% of small companies may not have in-house accountancy staff and therefore would not incur a training cost. This would reduce the one-off cost burden on this sector to £576m. It is estimated that the cost for medium to large companies may be between £3600 and £6000 per company (or between £270m (2 x £499 x 3 + 2 x £100 x 3) x 75,000) and £450m ((2 x £499 x 5 + 2 x £100 x 5) x 75,000) for the sector as a whole).

25. There may be additional on-going costs for small companies in having to comply with adopted IAS. IASB standards are primarily focused on the reporting requirements of large publicly traded companies which are involved in complex transactions. Some standards are irrelevant to small companies or require them to account for certain transactions in overly complex ways. As yet, there is no equivalent to the ASB's Financial Reporting Standard for Smaller Entities, which brings together in one place, with some simplifications, the accounting requirements from each of the full domestic standards as they apply to small companies. We would estimate the extra staff time spent in applying adopted IAS to be in the region of 1 person for 2 days per annum. Assuming the cost of staff time to be approximately £100 per day (a salary of £25,000 per annum), the cost of this may be approximately £200 per company (or £240m (£100 x 2 x 1.2m) for the sector as a whole). Again, if as many as 60% of small companies do not prepare their own accounts, the on-going cost burden would be reduced to £96m for the sector as a whole.

26. The Department is particularly interested to hear from small companies about the possible effect on them of the option of extending the Regulation to all companies.

27. The cost or benefit of extending the application of the Regulation will be dependent at least in part on the extent of convergence between UK accounting standards and adopted IAS. Consultees may wish to comment on the relationship between the costs and benefits of any extension to the application of the Regulation and the ASB's convergence programme in their particular case.

28. There is also the issue of whether companies should be permitted or required to comply with the application of the Regulation. Permitting companies to comply with the application of the Regulation would have no implementation costs because companies would not <u>have</u> to do anything. Requiring companies to comply with the application of the Regulation would

have costs to business dependant on the option chosen for extension of the application of the Regulation.

29. If the application of the Regulation was deferred to 2007 in two specific cases, those companies would benefit by having more time to prepare for using adopted IAS. However, the cost of compliance would be the same; it would simply be spread over an extra two years.

30. The table below shows the approximate number of companies affected by each option (please note that the numbers given are not cumulative) and a summary of the costs and benefits of each option. It assumes the companies covered by the Regulation have already committed all the relevant costs to implement the Regulation. Option 2(vi) has not yet been costed because of the difficulty in identifying the number of companies covered.

	Approximate number of companies affected	**Cost (£)**	**Benefit (£)**
Option 1	0	-	-
Option 2(i)	2,700	-	£5.4m approx per year
Option 2(ii)	27,000	-	Between £21m and £54m approx per year
Option 2(iii)	250	£1.5m approx in one-off training costs. There will be one-off IT system costs which have not yet been estimated.	Easier comparison across sectors and markets.
Option 2(iv)	75,000	Between £270m and £450m approx in one-off training costs. There will be one-off IT system costs which have not yet been estimated.	Easier to seek admission to trading on a regulated market. Easier comparison across sectors and markets.

Option 2(v)	1,200,000	Between £576m and £1440m in one-off training costs. Between £96m and £240m in on-going compliance costs. There will be one-off IT system costs which have not yet been estimated.	Easier comparison across sectors and markets.

Consultation

31. On 30 August, the Department announced that it was consulting on the extension of the application of the Regulation and published a consultation document. The consultation document was sent to around 1000 businesses, professional bodies, representative organisations and individuals. The deadline for comments is 26 November 2002.

Effect on Small Business

32. The summary in the table above shows the initial estimates of the costs and benefits to small businesses (Option 2(v)). These are discussed in more detail at paragraphs 21 to 25 above. The Department is particularly interested to hear from small companies about the possible effect on them of extending or not extending the application of the Regulation.

Monitoring and Enforcement of Compliance

33. In Great Britain there is already a well-regarded enforcement regime in place for ensuring that financial statements meet the requirements of existing legislation. Currently the Financial Reporting Review Panel (FRRP) has legal authority to review companies' accounts and if necessary to go to court to compel a company to revise its accounts. The FRRP shares this authority with the Secretary of State. By administrative agreement the FRRP deals with the accounts of large public and private companies, and the Secretary of State (through Companies House) with the rest. The Government's present intention is to retain this enforcement system for ensuring compliance with adopted IAS. Therefore, there will be no additional costs in setting up a new enforcement mechanism.

ANNEX E

CODE OF PRACTICE ON WRITTEN CONSULTATIONS

The following criteria apply to all UK national public consultations, and have been applied to this consultation paper.

1. Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
2. It should be clear who is being consulted, about what questions, in what timescale and for what purpose.
3. A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
4. Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others), and effectively drawn to the attention of all interested groups and individuals.
5. Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
6. Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and reasons for decisions finally taken.
7. Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated.

Responses to the consultation should be sent to the address given at paragraph 2.2 of the consultation document. If, however, you wish to make any comments about the handling of this consultation, please contact:

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Further information about this code of practice can be found at:
www.cabinet-office.gov.uk/servicefirst/index/Consultation.htm.

URN 02/1158