

# Consultation on the UK Implementation of the EU Accounting Directive: Chapters 1-9

## Consultation response

**24 October 2014**

CIPFA, the Chartered Institute of Public Finance and Accountancy, is the professional body for people in public finance. Our 14,000 members work throughout the public services, in national audit agencies, accountancy firms, public service organisations, charities and social enterprises and other bodies where public money needs to be effectively and efficiently managed.

As the world's only professional accountancy body to specialise in public services and public benefit organisations, CIPFA's portfolio of qualifications are the foundation for a career in public finance. They include the benchmark professional qualification for accountants working in public benefit organisations as well as a postgraduate diploma for people already working in leadership positions. They are taught by our in-house CIPFA Education and Training Centre as well as other places of learning around the world.

We also champion high performance in public services, translating our experience and insight into clear advice and practical services. They include information and guidance, courses and conferences, property and asset management solutions, consultancy and interim people for a range of public sector clients.

Globally, CIPFA shows the way in public finance by standing up for sound public financial management and good governance. We work with donors, partner governments, accountancy bodies and the public service providers around the world to advance public finance and support better public services.

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## **General Comment**

CIPFA welcomes the opportunity to respond to the consultation on the UK Implementation of the EU Accounting Directive: Chapters 1-9. This response focuses on the questions included in the consultation document.

In general, CIPFA welcomes initiatives aimed at reducing 'red tape' for small companies including the many charities and social enterprises that meet the criteria for classification as small companies. The consultation questions were circulated to members of CIPFA's Charities and Social Enterprises Panel and this response is informed by their comments and discussions.

While there is genuine concern over where exactly the balance lies in regard to simpler reporting and effective and informative reporting, we recognise that this is an ongoing and dynamic process and that the companies themselves have a role to play in deciding on their options for reporting to their stakeholders. As such we support a flexible approach while understanding that company reporting (both financial and non-financial) must continue to develop and respond to stakeholder demand for useful information on which to base their decisions and actions.

## **Responses to questions**

### **Question 1: Do you agree that the Government should maintain the UK's existing approach to financial reporting and only introduce changes where imposed by the Directive or where new options have been introduced?**

Yes. CIPFA supports, in general, the approach taken by the Government of introducing changes required by the Directive as well as considering potentially beneficial changes linked to the new options available.

### **Question 2: Do you agree that the Government should maintain the current position of providing discrete regulations for small companies and for large and medium-sized companies?**

Yes. We support the differentiation between small, medium and large companies, as a useful way for setting out requirements. In general, it reflects key differences in the resources available for each size and recognises that a one size fits all approach is inappropriate. Providing discrete regulations for small medium and large companies is also compatible with a 'think small first' approach, which the Directive identifies with.

### **Question 3: Do you agree it would be helpful to have a new set of Small Companies and Group Regulations which set out the new small company regime and incorporate both the small companies' exemption and the micro-entities exemptions clearly and in one place?**

No. We would prefer a more clear distinction between regulations for small entities and for micro-entities. We would welcome 'plain English' regulations and guidance for micro-entities which provide a comprehensive view of relevant requirements.

### **Question 4: Do you have suggestions for other regulations that might reasonably be consolidated as part of the implementation of this Directive?**

No.

### **Question 5: Do you agree that the new regulations should apply to financial statements for financial years commencing on or after 1 January 2016?**

Yes.

**Question 6: Should companies be able to access the new financial reporting regime (increased thresholds and revised reporting requirements) ahead of the mandatory application date of 1 January 2016?**

While early adoption has some attractions it may be that for practical reasons it would be better to wait for their implementation. The mandatory application date of 1<sup>st</sup> January 2016 provides sufficient time to develop appropriate guidance and information in support of the changes and to communicate this information to companies so that they have a good understanding of the options available to them.

**Question 7: Do you agree with the Government's proposal to maximise the small company thresholds and provide as many eligible companies as possible with the opportunity to access the small company regime?**

Yes. Our view is that this approach provides the greatest flexibility for small companies, while supporting a balance between the benefits and costs of financial reporting.

**Question 8: What benefits or costs do you think will arise from raising the company size thresholds?**

We note the academic research already done in this respect, and that BIS has already drawn on that body of work. We do not have any further comments, other than recognising the challenges of comprehensively identifying and evaluating all relevant benefits and costs.

**Question 9: Do you agree that the Government should continue to measure a company's size by reference to its balance sheet total, net turnover and average number of employees?**

Yes. It is an accepted and understood approach.

**Question 10: Do you consider that there are circumstances where the Government should include other sources of income as net turnover for the purposes of determining company size?**

There may be, but we believe that this would require further research and consultation.

**Question 11: Do you consider that there are circumstances (beyond those already in the UK accounting framework) where it would be appropriate to require:**  
**(a) parent undertakings to calculate their thresholds on a consolidated basis rather than an individual basis; or**  
**(b) "affiliated undertakings" to calculate their thresholds on a consolidated or aggregated basis?**

No. The existing approach to thresholds is relatively straightforward and such a change may result in additional resources being diverted purely to calculate a threshold.

**Question 12: Do you consider that there are circumstances where the Government should adopt either or both of the above provisions?**

No. Please see answer to previous question.

**Question 13: The Accounting Directive offers an option to reduce from 13 to 8 the number of mandatory notes required from small companies. Do you agree with the Government position to continue to require the five notes listed at paragraph 8.18?**

Yes.

**Question 14: Should the requirement for these notes be set out in regulations or should the need for notes be set out in accounting standards?**

We recommend the notes be set out in accounting standards, with possibly the exception of the requirement to disclose the registered office, which is an administrative requirement.

**Question 15: Do you agree that small companies should have the choice of preparing an abbreviated balance sheet and profit and loss account if they wish?**

In general we support providing small companies with the freedom to choose whether to prepare an abbreviated balance sheet and profit and loss account. While a case can be made in support of more extensive accounting, on balance, it would seem reasonable to allow small companies the option, while ensuring they understand and consider relevant benefits and costs associated with other options.

**Question 16: If small companies were permitted to prepare an abbreviated balance sheet and profit and loss account, please indicate if there are any line items which you would consider it essential to retain to support the presentation of a true and fair view of a company's financial position? Please explain.**

This requires further discussion with appropriate stakeholders in order to arrive at a shared accepted view on this. CIPFA would welcome engagement in such a discussion.

**Question 17: What benefits or costs might a small company see from deciding to prepare an abbreviated balance sheet and P&L? Evidence in support of your views would be helpful.**

As per question 8, we note the academic research already done in this respect, and that BIS has already drawn on that body of work.

**Question 18: What benefits do you believe this change will offer to small groups of companies? Evidence in support of your views would be helpful.**

Please see previous answer.

**Question 19: Should the Government only exclude from the small company accounting regime those public companies whose securities are traded on a regulated market?**

No. Public companies represent a distinct group and we believe the best approach is to treat them all as large companies.

**Question 20: Should the Government allow small companies who are members of a group which includes a public company to access the small companies regime?**

No. To allow small companies who are members of a group which includes a public company to access the small companies regime would be contrary to recognising their position as a member of a group which includes a public company.

**Question 21: Should the Government only exclude from the medium-sized company regime those public companies whose securities are traded on a regulated market?**

No. As per our answer to question 19.

**Question 22: Should the Government allow companies who are members of a group which includes a public company to access the medium-sized companies' regime?**

No. As per our answer to question 20.

**Question 23: Do you consider that the exclusions from the dormant subsidiaries accounting exemptions (where the subsidiary has a parent company guarantee) should be amended so that:**

**a) Companies are excluded because they have securities traded on a regulated market rather than because they are quoted companies?**

No

**b) Companies are excluded if they are part of an "ineligible group" under that definition as amended for the purposes of the small companies accounting regime?**

No

**Question 24: Do you agree that only permitting Formats 1 and 2 of the P&L should not impact significantly on UK companies?**

Yes

**Question 25: Should the UK take advantage of this option to provide greater flexibility in the layout(s)?**

Yes. We support flexibility in order to allow for sector specific layouts. An example of this is co-operatives, with members that will benefit from financial statements that reflect the distinct nature of their participation in and transactions with the co-operative.

**Question 26: If the UK took up this option, should flexibilities be dealt with in the regulations or in accounting standards and why?**

We believe that it would be appropriate to deal with them in accounting standards. Standards are the appropriate place for developing guidance on such accounting matters.

**Question 27: Do you agree that the legislation should enable participating interests to be accounted for using the equity method in individual company financial statements?**

We recommend that the regulations be designed to allow for the adoption of the relevant accounting standards that are applicable. This will allow for future developments in standards.

**Question 28: Do you agree that the Government should provide for the 10 year maximum period for write-off offered in the Accounting Directive?**

No. We believe that the existing maximum should be understood as the exception rather than the rule. In addition new requirements have already recently been established in FRS 102. In our view the case for extending the maximum has not been adequately made and therefore the existing maximum should be retained while allowing for further debate regarding the merits of the suggested 10 year maximum.

**Question 29: Do you agree that the removal of this option should take effect alongside other changes to the UK's financial reporting framework?**

Yes. It would seem reasonable for it to take effect at the same time.

**Question 30: Do you agree that the companies eligible to take advantage of the micro-entity regime should be relieved of the obligation to prepare a Directors' Report? What costs or benefits would result from this change?**

Yes, given the existing limited content required in a micro entity's Directors' Report.

**Question 31: Do you agree that the thresholds for the small companies audit exemption should remain unchanged for the time being i.e that the thresholds for the audit exemption should not be increased in line with thresholds for the small company regime for accounting purposes at this time?**

Yes. While ideally both small company accounting and audit thresholds should be dealt with together, we recognise the tight deadline for implementation of the Directive.

**Question 32: Do you consider that the exclusions from the small companies audit exemption should be amended so that:**

**a) Small companies are no longer excluded simply because they are public companies, though they are excluded if they have securities admitted to trading on a regulated market?**

**b) Small companies are only excluded if they are part of an "ineligible group" under that definition as amended for the purpose of implementing changes to the small companies accounting regime?**

a) No. As stated earlier we take the view that no public company should be allowed access to the small companies regime including small companies audit exemption.

b) No. The definition of an 'ineligible group' should not be amended to allow for use of the small companies regime.

**Question 33: Do you consider that the exclusions from the subsidiaries audit exemption (where the subsidiary has a parent company guarantee) should be amended so that:**

**a) Companies are excluded because they have securities admitted to trading on a regulated market rather than because they are quoted companies?**

**b) Companies are excluded if they are part of an "ineligible group" under that definition as amended for the purpose of implementing changes to the small companies accounting regime?**

No to both questions. In both cases, it is unclear that the benefits of the proposed changes have been clearly identified.

**Question 34: Do you consider that the exclusions from the dormant companies audit exemption should be amended so that:**

**a) Companies are excluded if their securities are traded on a regulated market?**

**b) Companies are excluded if they are part of an “ineligible group” under that definition as amended for the purpose of implementing the small companies accounting regime?**

Yes. We agree that companies with securities traded on a regulated market should be excluded.

No. We do not agree that companies should be excluded if they are part of an “ineligible group”. As per question 33, it is not clear that the benefits of such a proposed change have been clearly identified.

**Question 35: Do you agree that Article 28 (2)(e) of the Audit Directive, as inserted by Article 1 paragraph 23 of the Audit Directive 2014/56/EU, should be implemented with the changes included in the new Audit Directive?**

Yes.

**Question 36: Are there any other changes made to Article 28 of the Audit Directive under Directive 2014/56/EU that you consider should be implemented at the same time as the changes introduced with the insertion of Article 28 of the Audit Directive by Article 35 of the Accounting Directive?**

We have no suggestions regarding other changes.

**Question 37: Do you agree that the regulations should be amended to revoke the current requirement for disclosure of fees paid to auditors of medium sized companies for non-audit services?**

No. We would wish to encourage transparency on both audit and non-audit services provided by the auditor, given their role.

**Question 38: Do you agree that the current requirement for disclosure by large companies of fees they have paid to auditors for non-audit services should no longer be extended to small and medium sized public companies unless they have securities traded on a regulated market?**

No. As per previous answer.

**Question 39: Do you agree that the current requirement for disclosure by large companies of fees they have paid to auditors for non-audit services should no longer be extended to small and medium sized companies in the same group as a public company?**

No. As per previous answer.

**Question 40: Do you consider that the current requirement for disclosure by large companies of fees they have paid to auditors for non-audit services should continue to be extended to small and medium sized companies that are members of ineligible groups?**

No. As per previous answer.

**Question 41: Do you:**

**a) agree that the regulation should be amended so that the current exemption from the disclosure of non-audit fees paid by subsidiaries is no longer available to a subsidiary whose auditor is not the group auditor; or**

**b) think the exemption should be available to these subsidiaries where the total non-audit service fees paid to their auditor by all the companies in the group is disclosed in the notes to the consolidated accounts?**

We support (a)

**Question 42: Do you agree that there would be merit in specifically stating in regulations made under company law that the information provided in the notes to the financial statements of a company charity is not limited to the information required by the Accounting Directive?**

Yes. We agree that there is merit in the regulations stating that the information provided in the notes to the financial statements of a company charity is not limited to the information required by the Accounting Directive. This is because of the reasons already outlined in the consultation document.

**Question 43: Do you agree that the current flexibility in presentation of financial statements of charities, in particular the requirement for an income and expenditure account and to adapt the arrangement, headings and sub-heading of financial statements to reflect the special nature of the company's activities, should be retained?**

Yes. As with the flexibility in layout allowed to accommodate other sector specific features (as mentioned in question 25), we agree this flexibility for charities should be retained.

**Question 44: Do you agree that a threshold based on gross income is more appropriate than its turnover for company charities?**

Yes. Given the diverse nature of charity income including donations, gross income is a more appropriate measure.