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Dear Sir

### **ASB request for comment on the future of UK GAAP**

We welcome the opportunity to respond to the above named policy proposal.

#### **Our view in summary**

We believe the time has come for UK GAAP to move forward into the IFRS arena and that the Board's proposal to adopt the IFRS for SMEs is to be welcomed. While change inevitably brings a time of transition and discomfort we believe that it would be wrong to stay with current UK GAAP as it has become an unsustainable mix of converged and non-converged standards, is unwieldy and too complex for the typical entity in the UK.

Compared to UK GAAP, the IFRS for SMEs is shorter, well written in plain English and more manageable for the target population. However, there are some aspects of the Board's proposals that deserve challenge and comment as we set out below.

#### **Definition of publicly accountable**

While we agree that the Board should adopt the IFRS for SMEs' definition of publicly accountable we also believe that additional guidance is necessary to (a) explain what the definition means and (b) enable UK users to apply the SME in a consistent manner across various entities and industries. Guidance in the form of principles rather than checklists is preferred but guidance is definitely needed.

#### **SORPs**

We note the Board's reluctance to be seen to be interpreting IFRS but in our view this can be avoided. SORPs consist of a mixture of GAAP, application guidance and interpretation where there is no GAAP. It should be possible to update the SORPs by removing GAAP (which may be found in the relevant standards) and then eliminating interpretations as the issues are dealt with by amendments to IFRS. Renaming the SORPs as industry, in our case social housing, application guidance for IFRS would better reflect their purpose going forward. Users and preparers are likely to expect some sort of endorsement, such as negative assurance, from the Board for any such guidance that is produced.

#### **Public benefit entities**

We agree that a public benefit entity standard would benefit UK GAAP but note that it is not clear from the proposal whether the Board intends to overlay this standard onto the 3 tier model or to require a single tier for all that apply a public benefit entity standard. Our starting point is that we would prefer that each social landlord is able to adopt the same

standard as is the current scenario under UK GAAP. However, our view is that the 3 tier approach remains valid for public benefit entities as they can vary significantly in size from very large entities with listed debt through to very small entities with simple operations. For social landlords the scale of activities between the largest and smallest is significant, for example turnovers from £400 million to £5 million. For the largest social landlords, balance sheet values are in excess of £1 billion, there is considerable use of derivatives, private placements in the UK and USA, and substantial commercial activities. This difference in scale may mean that adopting the IFRS for SMEs without the option to adopt some elements of full IFRS to reflect this may lead to less transparency in reporting. It will depend on the Board's view as to whether any desire for consistency is driven by public accountability status or the sector within which the entity operates. The regulators for each of the sectors will no doubt have a view on this too.

Our preference would be for a public benefit entity standard to be a positive stand alone document, written from the perspective of public benefit entities, rather than a supplement to IFRS for SMEs. In this case we believe that three documents would be required – the IFRS for SMEs, the PBE Standard and the social housing SORP (or equivalent).

Three of the main areas of relevance to public benefit entities that are not well served by IFRS are presentation, non-reciprocal transactions and control. The issues included within the proposal are relevant examples of these. The social housing sector is currently considering in great depth a number of these issues particularly the gift of control of one business to another for nil consideration and would welcome further guidance in this area.

### **Legal and regulatory issues**

There are clearly some legal and regulatory issues that need finalisation before being able to change UK GAAP including whether the IFRS for SME is compatible with the EU directives. There are other practical issues to be considered such as whether entities can move between the proposed tiers. Currently entities can move easily from UK GAAP to IFRS but not the other way, a reflection of the IFRS convergence agenda pursued to date. Our impression is that the Board is comfortable with entities moving between tiers as their circumstances change and we believe that the legal framework should allow this. There is also the issue of taxation and how movement between tiers for the first time and subsequently will be treated. While the Board should rightly concentrate on achieving the best accounting framework, information on these points will be valuable for entities making their decision as to which tier to apply,

### **Timing**

We are in favour of the Board's 2012 timetable although believe this is challenging. The additional work that is clearly required to incorporate SORP guidance and address public benefit entities may mean that PBEs make the move at a slower pace than corporate entities. This could be addressed by delaying a mandatory move while allowing early adoption from 2012. The Board should also monitor the IASB's stated plans to consider implementation issues and any improvements to the IFRS for SMEs in 2012 as it would be unhelpful if UK entities had to make significant changes shortly after adoption.

Our answers to your specific questions are included in the attached appendix.

Yours faithfully

## APPENDIX

### Question 1

*Which definition of Public Accountability do you prefer: the Board's proposal (paragraph 2.3) or the current legal definitions (paragraph 2.5)? Please state the reasons for your preference. If you do not agree with either definition, please explain why not and what your proposed alternative would be?*

Our preference is for the Board's proposed definition in paragraph 2.3. The Board's definition is more succinct and relevant to the target population. However it is clear to us that additional guidance is needed, either from the IASB or the Board, regarding applying the definition of publicly accountable in practice.

### Question 2

*Do you agree that all entities that are publicly accountable should be included in Tier 1? If not, why not?*

Based on the Board's definition we agree that publicly accountable entities should fall into tier 1.

### Question 3

*Do you agree with the Board's proposal that wholly-owned subsidiaries that are publicly accountable should apply EU adopted IFRS? If not, why not?*

Regardless of the group structure, if an entity is itself publicly accountable it should fall within Tier 1.

We recommend the Board clarifies the classification of a group as publicly accountable or not when it has a parent entity that is not publicly accountable but a subsidiary that is.

### Question 4

*Do you still consider that wholly-owned subsidiaries that are publicly accountable should be allowed reduced disclosures? If so, it would be helpful if you could highlight such disclosure reductions as well as explaining the rationale for these reductions.*

No specific comments to make.

### Question 5

*Do you agree with the Board's proposal that the IFRS for SMEs should be used by 'Tier 2' entities?*

Yes.

### Question 6

*Do you agree with the Board's proposal that the IFRS for SMEs should be adopted wholesale and not amended? If not, why not? It would be helpful if you could provide specific examples of any amendments that should be made, as well as the reason for recommending these amendments.*

In general we believe that the Board should adopt the IFRS for SMEs in full without any amendment. There may however be some areas where an opt out from the requirements of the IFRS for SMEs sector in favour of options given by full IFRS would be sought by the, for example on the capitalisation of interest or the choice between historic cost and valuation for housing property assets.

### Question 7

*Do you agree with the Board's proposal that large Non-Publicly Accountable Entities should be permitted to adopt the IFRS for SMEs? Or do you agree that large entities should be required to use EU adopted IFRS? Please give reasons for your view.*

Yes, we agree that whether or not an entity is publicly accountable is key, not its size.

We have noted that the phrases “publicly accountable” and “public interest” while meaning different things were often used inter-changeably during our conversations with users and preparers.

For those entities that are not publicly accountable but are considered to be of public interest we believe it is for regulators to decide whether the use of IFRS should be mandated rather than the Board amending their definition to suit. The flexibility to move up the Tier hierarchy would allow a regulator to impose IFRS while still complying with the Board's framework.

#### Question 8

*Do you agree with the Board that the FRSSE should remain in force for the foreseeable future?*

No specific comments to make.

#### Question 9

*Do you agree that the FRSSE could be replaced by the IFRS for SMEs after an appropriate transition period, following the issuance of the IFRS for SMEs?*

No specific comments to make.

#### Question 10

*Do you agree with the Board's current views on the future role of SORPs. If not, why not?*

During the course of our consideration of the Board's proposals regarding public benefit entities and SORPs it has become clear that this is probably the most complicated part of the proposal.

Individually the SORPs work very well for their sectors. The challenges faced by the Board are in moving toward IFRS and aligning the differences in SORP guidance that might exist between sectors.

When looking at the content of a SORP it can be split into three areas, GAAP, application of GAAP and interpretation where there is no GAAP. By removing any GAAP information, on the grounds that reference can be made to the underlying standards you are left with a document that provides guidance on the application of GAAP for a specific sector as well as additional GAAP where the underlying standards have yet to address the issue. Such a document could be renamed as application guidance for specific sectors and as and when IFRS or IFRS for SMEs is expanded or improved the SORP content can be reduced appropriately.

#### Question 11

*Do you agree with the Board's proposal to develop a public benefit entity standard as part of its plans for the future of UK GAAP? If not, how should (converged) UK GAAP address public benefit entity issues?*

Yes. See main body of our response for further detail.

#### Question 12

*If you do agree with the proposal to develop a public benefit entity standard, should the standard cover all the requirements for preparing true and fair view accounts or should it cover only those issues where IFRS or the IFRS for SMEs needs to be supplemented for the public benefit entity sector?*

Our preference would be for a public benefit entity standard that covers all requirements for preparing true and fair view accounts, subject to any matters covered in the supplementary sector specific guidance that is currently found in the SORPs. If the public benefit entity standard is produced as a supplement to IFRS for SMEs, then this would require preparers of the financial statements to refer to three documents. As we discuss in our response to question 10, IFRS for PBEs would need to be supplemented by sector specific guidance / SORPs. We do not believe that it would be practical to try and incorporate all of the SORP content into the public benefit entity standard given the number of stakeholders involved across these sectors, the different issues that they face and the differing approaches that they sometimes adopt in respect of similar transactions.

However, we would note that there will be issues (as there are now) with different accounting regimes between the parent entity and subsidiary companies, especially where they vary in size and accounting regime.

#### Question 13

*Do you agree the issues listed in the above table are distinctive for the public benefit entity sector and should therefore be covered in a public benefit entity standard? What other issues might the proposed standard include?*

The three main areas of relevance to public benefit entities that are not well served by IFRS are presentation, non-reciprocal transactions and control. The issues included within the proposal are relevant examples of these.

#### Question 14

*The Board accepts there may be a continuing need for guidance to supplement a public benefit entity standard in sectors such as charities, housing and education. Where this is the case, do you think the Board should provide a Statement confirming the guidance is consistent with UK GAAP, including the public benefit entity standard?*

As noted in our response to question 10 above supplementary guidance for certain sectors is likely to be necessary and assurance from the ASB that these are GAAP compliant would be desirable not only for public benefit entities but also for those profit seeking entities.

#### Question 15

*If you are an entity whose basis of preparing financial statements will change under these proposals, what are the likely effects of applying those new requirements? Please indicate both benefits and costs and other effects as appropriate. If you are a user of financial statements (such as an investor or creditor) what positive and negative effects do you anticipate from the implementation of the proposals set out in this paper?*

No specific comments to make.

#### Question 16

*What are your views on the proposed adoption dates?*

Our view is that the IFRS for SME is a sensible replacement for UK GAAP and is consistent with the Board's IFRS convergence agenda and so should be implemented on a timely basis. From the perspective of changing from UK GAAP to IFRS for SME a three year period running to 2012 seems sufficient time for entities to prepare and implement.

We would however note that the plans for public benefit entities still need further clarification and that there are a number of stakeholders in these sectors that will need to be consulted and potentially approve the ASB's proposals for the entities that they regulate. The timetable for public benefit entities may therefore differ from that for IFRS for SMEs.