The Quoted
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Accounting Standards Board
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3 May 2011

Dear Ms. Sansom,

**Accounting Standards Board – The Future of Financial Reporting**

***INTRODUCTION***

The Quoted Companies Alliance (QCA) is a not-for-profit membership organisation working for small and mid-cap quoted companies. Their individual market capitalisations tend to be below £500m.

The QCA is a founder member of European**Issuers**, which represents over 9,000 quoted companies in fourteen European countries.

The QCA Financial Reporting Committee has examined your proposals and advised on this response. A list of committee members is at Appendix A.

***RESPONSE***

We welcome the opportunity to respond to this consultation.

In our view, the overriding aims of any review of UK GAAP should be to introduce proportionate and differential reporting requirements that balance the needs of users with the costs of compliance and to reduce complexity where possible.

To this extent there are many elements of the Board's proposals to be welcomed; the FRSME is, in general, significantly less complex and easier to apply than current UK Financial Reporting Standards whilst the multi-tiered framework facilitates a targeted approach to meeting the differentiated needs of users.

However, we do have concerns with the way the tiers are determined and some of the detailed requirements of the draft standard. We also do not believe that the new framework should be introduced in the proposed timeframe and urge the ASB to not rush the development and implementation of the new framework.

**Gold-plating of company law**

We agree with the Board that "use should be made, where possible, of existing exemptions in company law to avoid gold-plating". However, we would also apply this philosophy to the application of the three-tier framework.

The proposed framework effectively "gold-plates" company law by requiring the application of EU-adopted IFRS by many entities currently outside of the IAS Regulation. By doing so, the Board is increasing the regulatory burden on such entities at a time when the Government is rightly looking to reduce regulation to foster growth.

The framework is predicated on the IASB's assertion that the IFRS for SMEs is not suitable for publicly accountable entities. We would urge the Board to act independently of the IASB and to be mindful that the IASB's assertion does not appear to be based on a rigorous analysis.

Furthermore, we do not agree with that all listed entities are publicly accountable or, on cost/benefit grounds, should be required to apply EU-adopted IFRS. In particular, we do not agree that all pension schemes, irrespective of size, should fall within Tier 1, nor do we understand why EU-adopted IFRS has been mandated for Employee Benefit Trusts when they are not required to publish general purpose financial statements.

Given Tier 2 entities have the option to apply EU-adopted IFRS, it should be left to market or industry regulators or market pressure from stakeholders to expand the scope of IFRS beyond that set out in Company law not the ASB.

**Extent of amendments to the IFRS for SMEs**

Whilst we agree that the IFRS for SMEs is a sound starting point for developing a simplified financial reporting standard for domestic application, we urge the Board to consider and make any amendments to it that result in requirements that are proportionate to the nature of the entities applying the standard, best meet the needs of domestic users and retain those established accounting practices that continue to result in relevant and reliable information. We do not consider the current guideline that "changes should be minimal" should take precedence over the development of a high quality financial reporting standard.

**Timing of changes**

We agree that there should be at least an 18 month gap between the issue of a final standard and its effective date. However, we do not believe an effective date of 1 July 2013 is achievable or desirable. We urge the Board not to rush the development of a new standard but to consider carefully the views of respondents and the impact and timing of developments such as the IASB's projects to revise IFRS and the IFRS for SMEs, initiatives to revise European Accounting Directives and the UK Government's growth agenda.

We are concerned that the conflict between the terminology and financial statement presentation set out in the Accounting Directives and those set out in the FRSME and, for qualifying subsidiaries, EU-adopted IFRS will create significant complexity in the preparation of financial statements under the new framework. It will also undermine the stated benefit of having one "accounting language" and public acceptance that the changes are beneficial.

We would urge the Board, alongside the Department for Business, Skills and Innovation, to lobby for change at the European level to encourage greater flexibility in the Accounting Directives so the FRSME terminology can be applied. Similarly, we would urge the Board to influence the IASB to develop a disclosure exemption regime for subsidiaries and the separate accounts of parent companies.

If publication and/or application of the FRSME and the new multi-tier framework is delayed until such wider initiatives are completed it will ensure a smoother and more successful transition and mitigate the effect of repeated changes in financial reporting practices.

**Needs of users**

We recognise that it is often difficult to identify the precise needs of users, particularly those that will use the financial statements of entities within the scope of the proposed FRSME. However, their views are critical to determining whether any new framework or detailed requirements are appropriate and we urge the Board to continue with its determined approach to canvassing their views.

Recent developments in financial reporting have been more influenced by theoretical or academic consistency than the usefulness or reliability of the information presented. In particular, we urge the Board to seek the views of users on the usefulness of recognising and measuring equity-settled share based payments, particularly by unquoted companies, recognising and measuring deferred tax assets and liabilities and fair valuing derivatives, with or without hedge accounting, such as forward foreign exchange contracts entered into to fix the purchase cost of a non-monetary asset.

We firmly believe that the Board should take the opportunity to review, rebalance and refocus the contents of financial statements, placing much greater emphasis on how they are used in practice. Consistent with the FRC's aims in its Cutting Clutter project, the Board should take this opportunity to fundamentally and critically review the usefulness of the measurement, recognition and disclosure requirements of any new standard. In line also with the FRC's Cutting Clutter project, we believe that the Board should consider how materiality could be most helpfully described and applied in order to ensure that financial statements are understandable and accessible for principle users.

***RESPONSES TO CONSULTATION QUESTIONS***

***The tier system***

***Q1 Do you agree that a differential financial reporting framework, based on public accountability, provides a targeted approach to relevant and understandable financial information that contributes to discharging stewardship obligations?***

We believe a differential reporting framework is essential in providing a targeted approach to the provision of relevant and understandable financial information, such that the needs of users are properly balanced with the costs of compliance.

However we do not agree that the proposed distinction between tiers 1 and 2 is the most appropriate one. In our view, the case for barring all publicly accountable entities from applying the FRSME has not been made.

The Board is charged with developing and maintaining UK Financial Reporting Standards and should not be tied by the decisions made and positions taken by the International Accounting Standards Board when it developed the IFRS for SMEs. As set out in the Alternative View, there is no analysis or evidence to support the IASB's assertion that the IFRS for SMEs is unsuitable for any and all publicly accountable entities.

In our view, the FRSME is, in general, appropriate to the needs of smaller quoted companies and their investors.

By requiring all publicly accountable entities to apply EU-adopted IFRS, the board is effectively "gold-plating" the requirements of European Law and the Companies Act, which only mandates their application by companies listed on a regulated market. Elsewhere in the consultation documents, the Board has justified amending the FRSME on the grounds of avoiding gold-plating so we do not understand why, when determining the financial reporting tiers, the Board is willing to go beyond the legislative requirements and place additional regulatory burdens on, for example, PLUS-quoted companies, who are able to currently opt to use UK GAAP but under the new regime will have to use full IFRS.

We believe the distinction between Tiers 1 and 2 should reflect the current EU Regulation on the application of EU-adopted IFRS, i.e. Tier 1 should be restricted to those companies listed on a regulated market.

***Q2 Do you have any further comments on the proposed application of the tier system?***

No response given as not relevant to our constituents

***Q3 Appendix 1 'Note on the Legal Requirements in the United Kingdom and Republic of Ireland' to this FRED sets out a note on legal matters that are applicable to the tier system. Do you have any comments or queries on the scope or content of this Appendix?***

We recognise the need for Appendix 1 and the need to consider the interplay of the FRSME, IFRS and the Accounting Directives but would highlight it is unfortunate that such complexity is required. We would urge the ASB to work alongside the Department for Business, Innovation and Skills to press for a European solution to these problems and, if necessary, delay the implementation of the new framework whilst these problems are resolved.

We are particularly concerned that the conflict between the terminology and format of IFRS and FRSME compliant accounts is not clearly set out in the FREDs. In our view a subsidiary applying the proposed reduced disclosure regime will be required to follow the Companies Act/Accounting Directives format and terminology, thereby creating differences in the overall presentation of the financial statements of subsidiaries compared to the full IFRS group accounts.

It has been argued by some that the terminology in the FRSME should be changed to make it consistent with the formats in Company law. Whilst this might improve understandability in the short-term, we believe consistency with IFRS terminology will in the longer term provide a stronger foundation for arguing at the European level for changes in the Accounting Directive or for a reduced disclosure framework to be incorporated into EU–adopted IFRS.

In the meantime, we would urge the board to provide straightforward but detailed guidance on the interaction of the new accounting framework and Company law.

***Entities with public accountability (Tier 1)***

***Q4 Should entities that have public accountability, satisfy all three of the size conditions of a small company or small group, and are prudentially regulated, be permitted to apply the FRSME?***

We welcome the exemption from applying EU-adopted IFRS given to small prudentially regulated publicly accountable entities.

However, such an exemption would not be required if the Board was not effectively proposing an extension to the EU IAS Regulation.

The Board's decision to offer this exemption indicates that the absolutist position taken in the IFRS for SMEs (that it is not appropriate for any publicly accountable entities) is open to challenge. We believe the Board should consider whether more publicly accountable entities be permitted to apply the FRSME. As discussed above in our response to Question 1, we believe it unnecessary to use public accountability as the defining characteristic to distinguish between tiers and propose that Tier 1 be restricted to those entities that, under EU legislation, are already required to apply EU-adopted IFRS.

***Q5 Are the definition of public accountability and the accompanying application guidance sufficiently clear to enable an entity to determine if it has public accountability? If not, why not?***

In addition to our concerns on extending the scope of full IFRS to AIM and PLUS quoted companies, we also believe the application guidance includes entities which are not, in our view, publicly accountable.

One of the key problems with the IFRS for SMEs definition of publicly accountable is the imprecision of the term "a broad group of outsiders". We do not agree with the interpretation and application of this term set out in Appendix 2 of FRED 43.

In particular we do not consider all pension schemes to have public accountability. To require even the smallest of pension schemes to apply EU-adopted IFRS does not, in our opinion, satisfy any cost/benefit analysis. We do not agree with the assertion in section 11 of the Explanation that changes to their accounts will be minimal as this ignores, for example, the requirement to present the disclosures set out in IFRS 7.

If it is in the public interest for some pension schemes to prepare accounts in accordance with EU-adopted IFRS, then this could be imposed by the Pensions Regulator. Similarly, other regulators such as the FSA or Bank of England could impose EU-adopted IFRS on other entities of sufficient public interest if Tier 1 was limited to those with instruments traded on regulated markets.

Similarly, we do not agree with the inclusion of EBTs in the list of publicly accountable entities. Not only are many such entities small with very few beneficiaries, they are not required to prepare or publish general purpose financial statements.

We would also urge the board to clarify that entities that do not recognise client assets on their balance sheet because, for example, they are held by a separate nominee or custodian are not publicly accountable as the client is not exposed to the risk of failure of the entity.

***Q6 The ASB is proposing to amend the IFRS for SMEs to comply with Company law. Do you agree with the amendments? If not, please explain your reason for disagreement and, if appropriate, suggest an alternative.***

We agree with the proposed amendments to the IFRS for SMEs to comply with Company law. However we would note that changes have not been made where Company law permits accounting policies that are not

permitted by the IFRS for SMEs. We believe further amendments are necessary so entities applying the FRSME may retain accounting policies (such as the revaluation of tangible fixed assets) permitted in law and consistent with EU-adopted IFRS, but barred by the IFRS for SMEs.

***Q7 The ASB decided to evaluate possible amendments to the IFRS for SMEs using three guidelines:***

***(a) changes should be minimal;***
***(b) changes should be consistent with EU-adopted IFRS; and***
***(c) use should be made, where possible, of existing exemptions in Company law to avoid gold-plating.***

***Do you agree with these guidelines? If not, please explain why.***

We do not consider the apparent prominence given to ensuring "changes should be minimal" to be appropriate and we believe it has deterred the Board from making important improvements to the IFRS for SMEs. For example, adding an option to revalue property, plant and equipment would make the FRSME more consistent with EU-adopted IFRS, would permit the use of an option already allowed by Company law and empower preparers to make their own cost/benefit analysis of following such an accounting policy in light of their users expressed needs. It appears that the only rationale for not introducing revaluation is point (a) above.

Changes should be made if and only if, when they are subjected to thorough analysis, they would result in a financial reporting standard that best meets the needs of preparers and users. Such an analysis would place a proper limit on the number of changes.

The primary objective of the Board at this time should be to produce a high quality financial reporting standard for application in the UK by those entities falling outside the EU IAS Regulations that is less complex and burdensome than both current UK GAAP and EU-adopted IFRS. The IFRS for SMEs provides a useful starting point for such a standard, but should be adapted wherever changes would lead to improvements.

We are not persuaded by arguments that international harmonisation requires that changes be kept to a minimum. The majority of businesses that will apply the FRSME will not generally be subject to international comparisons. Where international comparisons are made, these are most likely to be with European competitors, which would not necessarily apply the IFRS for SMEs.

We also note that some of the simplifications introduced by the IASB in developing the IFRS for SMEs are not needed in the UK, which has a highly developed accounting profession and sophisticated users. For example, there is an established practice of permitting revaluation of property, plant and equipment, which should be maintained.

We propose that more appropriate guidelines for evaluating amendments to the IFRS for SMES would be:

(a) Changes result in financial reporting requirements that are proportionate to the nature of businesses applying the standard that best meet the needs of domestic users and evolve from established practices;
(b) Subject to (a), changes result in greater consistency with EU-adopted IFRS

***Q8 The ASB has amended the IFRS for SMEs to:***

***(a) replace section 29 Income Tax with IAS 12 'Income Taxes';***
***(b) provide transitional relief for dormant entities with intra-group balances;***
***(c) exempt an entity preparing consolidated financial statements from including a parent company cash flow statement; and***
***(d) revise the scope of section 9 such that an entity is required to prepare consolidated financial statements only when required to do so by Company law.***

***Do you agree with the amendments? If not, please explain your reason for disagreement and, if appropriate, your proposed alternative.***

Whilst we agree that section 29 should not be applied in its current form, we do not agree with its replacement by IAS 12 which is to long and too onerous. We expect that the relevant section of IFRS for SMEs and IAS 12 will both be replaced in the near future.

We would urge the Board to consider alternative approaches to accounting for deferred tax, including flow-through or some form of partial provisioning, and to canvass users views on these alternatives. In our experience, many users ignore current deferred tax items and would be better served by disclosures in the notes of financial statements that explain differences between the tax charge and a standard rate of taxation in the current year and information to predict differences in the near future.

We agree with the amendments (b), (c) and (d) as listed above and suggest further amendments in our response to question 24.

***Small entities (Tier 3)***

***Q9 Do you agree with the proposed consequential amendments to the FRSSE? If not, why not? Please state your reason for disagreement and, if appropriate, suggest an alternative.***

No response given as not relevant to our constituents.

***Reduced disclosures for subsidiaries***

***Q10 The ASB is proposing that subsidiary undertakings which apply the reduced disclosure framework should:***

***(a) disclose the disclosure exemptions taken;***
***(b) state in the notes the name of the parent undertaking in whose consolidated financial statements the subsidiary's results and relevant disclosures are included; and***
***(c) only be permitted to take the disclosure exemptions where the consolidated financial statements of the parent are publicly available.***

***Are these requirements necessary and sufficient to protect users of subsidiary financial statements?***

We agree these requirements are necessary and sufficient to protects users of subsidiary financial statements.

***Q11 The ASB proposes that disclosure exemptions should be permitted for all subsidiary undertakings: do you agree, or do you consider that there should be a minimum percentage ownership requirement?***

We agree that the disclosure exemptions should be permitted for subsidiary undertakings unless shareholders require otherwise. However, we consider that any request to provide full disclosure should be supported by at least 10% of shareholders. This minimum purchase ownership requirement has been set in reflection of the level set for compulsory purchases of listed company minority interests.

***Q12 Do you consider that a disclosure exemption should or should not be provided for transactions between wholly-owned group undertakings? Please explain your reasoning.***

Whilst a disclosure exemption remains in Company law, the standard should also provide an exemption from providing disclosures on transactions between wholly-owned group undertakings.

***Q13 The reduced disclosure framework was developed in response to the feedback on the ASB's policy proposal issued in August 2009. Qualifying subsidiaries applying the reduced disclosure framework look to EU-adopted IFRS and the Appendix to the draft Application FRS to prepare their financial statements. Does this proposal adequately address preparers' needs?***

We welcome the reduced disclosure framework for qualifying subsidiaries, but believe more detailed and straightforward guidance is required to aid users in their application of EU-adopted IFRS within the Companies Act's financial statement formats and terminology.

It is unfortunate that Appendix 1 is so complex, but we recognise this is unavoidable given the conflicts between IFRS and the Accounting Directives. We urge the Board to work with BIS at a European level to address these issues and to consider delaying a change to the UK financial reporting framework as the project to revise the Accounting Directives develops.

**Q14 Do you have any further suggestions for disclosure exemptions for qualifying subsidiaries? If so, please explain why you consider the disclosure is not required in the subsidiary financial statements.**

We would extend many of the disclosure exemptions to the separate financial statements of the parent company, especially where the argument for providing exemptions to subsidiaries is that the matters are managed on a group basis. The Board should be mindful of the FRC's Cutting Clutter project and ensure that as far as possible unnecessary and repetitive disclosure requirements are removed, potentially through exploring how materiality could be most helpfully described and applied.

***Draft impact assessment***

***Q16 Do you agree with the benefits that have been identified as arising after adoption of the proposed Financial Reporting Framework? If not, why not? Please provide examples, including quantification where possible, of any benefits you believe have not been taken into account.***

As outlined in our Corporate Reporting Charter (attached to the end of this document), we are committed to working with standard-setters to promote high quality financial reporting by quoted companies. In order to conclude whether the proposed Financial Reporting Framework provides this benefit, in our view, the ASB needs to have a clearer view of who are the users of the accounts.

As such, we do not believe that the benefits outlined in the draft impact assessment are properly quantified or outlined, especially as many of them are qualitative in nature.

Firstly, the costs of transition noted in section 11.25 of the consultation document are estimated to be £78.9m; however, it not clear how this number was calculated.

In addition, while the costs have been estimated, it appears that they may be understated. For example, there is insufficient justification to assume that entities will benefit from a reduction in cost – in fact, we do not consider it reasonable to analogise to the experience of large listed groups.

We would suggest that the cost calculations should be carried out by appropriately segmenting constituents and assessing the costs/benefits in relation to smaller listed companies and AIM/PLUS-quoted companies from FTSE 350 companies, where benefits to the capital markets from the use of IFRS are likely to be much greater. For example, the cost calculations carried out for the draft impact assessment would have assumed that the lowest qualified person in a company would do the task of preparing accounts under the new regime; however, in smaller quoted companies it usually a very highly qualified person, e.g. the finance director, undertaking this task, which would push implementation costs up. In addition, we believe that any analysis of the cost should recognise that these changes would not just generate costs from the perspective of finance departments in companies. It would also affect Human Resources and Sales Departments, for example, resulting in costs and training.

Additionally, we do not believe that the costs of implementation have been properly analysed for publicly-accountable entities, which definition has been widened in the proposed framework. For example, PLUS-quoted companies currently can use UK GAAP and so the costs of implementation of moving to full IFRS, as proposed under the new tier system, would be very high.

Secondly, we do not agree with the analysis that these framework changes will lead to a reduction in the cost of lending and borrowing. Given the current financial environment, we would challenge this statement and believe that the costs will only increase. It is not uncommon for lenders to try and raise costs via refinancing fees where covenants are either broken or have to be renegotiated or where there is perceived volatility. This is likely to delay any benefit being enjoyed and could feasibly increase costs as many companies renegotiate their banking covenants as a result of the tier 2 accounting requirements.

Thirdly, although we would agree that implementation of these proposals will result in all accounting being based on an IFRS-based framework, we believe that there is still scope for confusion arising from the various

reporting tiers. In addition, for UK subsidiary companies we would not expect comparison with competitors to be of any benefit.

***Q17 In relation to the case study scenarios identifying the likely costs of transition for certain entities, do you agree with the nature and range of costs identified? If not, please provide details of any alternatives you would propose, including any comments on the assumptions underlying the calculation of the costs.***

The case study scenarios which are relevant for the majority of our members are company E in relation to parent company financial statements and scenario D2 for subsidiaries.

As outlined in Question 16, we anticipate that the proposals could also result in an increased amount of the finance team's time being taken up for tax accounting and reporting and implementation of changes to business processes and controls as well as training or, where a company's resources may be limited, increased cost of using external advisers. In our opinion the cost estimates outlined in the case study scenarios would appear to be understated for our members.

We do not agree that time and cost will be saved in the audit function in relation to subsidiaries due to the additional fees for audit of the transition process and comparative financial information.

***Q18 The [draft] Impact Assessment also gives an indication of the impact on the 'main affected groups'. Do you agree with this analysis? If not, why not?***

As outlined in Question 16, we suggest there should be appropriate segmentation in the cost/benefit impact assessment, in that the assessment of smaller listed and AIM/PLUS-quoted companies should be dealt with separately from that of FTSE 350 companies where benefits to the capital markets from the use of IFRS are likely to be much greater.

***Q19 The benefits are hard to quantify; do you agree that they outweigh the costs of transition and any ongoing incremental costs? Do you have any comments on the estimates used?***

With so many potentially new IFRSs in the course of drafting at present, we are increasingly not persuaded that the benefits outweigh the costs of transition and ongoing incremental costs. A number of the IASB proposals in IFRS literature in the course of preparation are controversial and potentially would add significant costs for preparers.

***Q20 The ASB is proposing an effective date of July 2013, with early adoption permitted, which assumes an 18 month transition period. The ASB's rationale for this date is set out in paragraphs 11.121 to 11.126. Early adoption will permit entities to secure benefits as soon as possible, however other entities may wish to defer the effective date to permit businesses more time to prepare for transition. Do you agree with the proposed effective date and early adoption? If not, what would be your preferred date, and why?***

As mentioned in our response to Question 1, we are not convinced of the need for change in the tight timeframe provided in this consultation. We believe that there needs to be more engagement with users of accounts to ensure that the FRSME is developed into a standard that meets their needs and also to allow for an in depth segmented cost/benefit analysis to be undertaken.

We consider particular care should be taken at present, while growth of the economy remains fragile, not to detract finance directors and their teams from focusing their efforts on growing their businesses in a sustainable fashion. In our opinion significant accounting changes, unless they will bring very demonstrable net benefits to preparers and/or users of financial statements, should not be introduced without sufficient evidence to support the argument that UK GAAP is outdated.

***Q21 Please provide any other comments you may have on the [draft] Impact Assessment.***

We believe the ASB should have detailed discussions with the major users of the financial statements of smaller listed and AIM/PLUS-quoted companies to ascertain what information they need and actually use. This will ensure proposals for this group of companies are properly evidence based.

***Alternative view***

***Boundary between Tier 1 and Tier 2***

***Q22 Do you agree that all the entities that the ASB has identified as falling within Tier 1 should be in Tier 1, or do you agree with the Alternative View that some could move to other tiers? If you do think some entities could be moved– which entities and to which tier?***

As discussed above, we do not agree with the ASB proposal to mandate the application of EU-adopted IFRS to entities currently outside the scope of the EU IAS Regulations. Such entities currently within Tier 1 should be moved to Tier 2 unless they are permitted to apply the FRSSE.

We believe market pressure, be it expressed by stakeholders or regulations such as the AIM Rules, will result in the voluntary adoption of EU-adopted IFRS, where it is appropriate and beneficial to users.

Incidentally, we would urge the Board to make further representations to the Department for Business, Innovation and Skills to amend the current restrictions on AIM/PLUS-quoted companies that delist from choosing to apply UK GAAP because they are effectively treated as voluntary adopters of IFRS.

***Q23 Are you aware of any information that users of financial statements of publicly accountable entities require which would not be disclosed in financial statements prepared using the FRSME (the IFRS for SMEs adapted for use in the UK)? If so, please identify such information and explain why it is required.***

Whilst we consider stakeholder pressure would generally be applied should users legitimately require the adoption of EU-adopted IFRS, we do consider it necessary for the disclosure of information on operating segments and earnings per share should a publicly traded company be permitted to apply the FRSME in accordance with the Alternative View.

***Accounting requirement for entities falling into Tier 2 (FRSME)***

***Q24 Do you believe that the ASB's proposals for the FRSME should be changed to reduce complexity? If so, what changes would you suggest? Please explain how such changes would improve the balance between costs and benefits.***

In addition to the amendments proposed by the Board, and consistent with our proposed guidelines for making amendments to the IFRS for SMEs, we would propose the following amendments:

(a) The introduction of an option to apply a revaluation model to the measurement of property, plant and equipment, consistent with IAS 16;
(b) The introduction of an option to capitalised borrowing costs into the cost of qualifying assets. Whilst IAS 23 requires such capitalisation, an option to do so will allow the application of policies consistent with EU-adopted IFRS whilst still providing flexibility for individual entities to best meet the needs of users of their financial statements;
(c) The introduction of an option capitalise development costs where criteria such as those set out in IAS 38 are met. Again, this will allow the application of policies consistent with EU-adopted IFRS whilst still providing flexibility for individual entities to best meet the needs of users of their financial statements;
(d) The introduction of a restricted option to avoid fair valuing of certain derivatives to reflect the business rationale for entering into them without the need for complex and costly hedge accounting. For example, where a forward exchange contract is entered into to fix the functional currency cost of an asset purchase, we consider it appropriate to recognise the asset at acquisition at the contracted rate without previously recognising the derivative at fair value. This approach would be similar to that currently set out in paragraph 4 of SSAP 20 and could be supplemented by requirements to provide full disclosure of contracts in place at the reporting date. Similar arguments could be put forward for the use of contracted rates on interest rate swaps without the need to introduce the volatility associated with fair valuing.

We would urge the Board to also consult with users on the usefulness of the financial reporting of other areas, such as equity-settled share-based payments and defined benefit schemes. This consultation could be done in light of the FRC's Cutting Clutter project.

***Q25 If the FRSME was changed in accordance with your response to Q24, would it still be suitable for use by some publicly accountable entities? If not, why not?***

We consider the amendments to the FRSME we have put forward in this response would still result in a standard suitable for use by some publicly accountable entities.

***Boundary between Tier 2 and Tier 3***

***Q26 The current cut-off point for the FRSSE is the small company threshold (Turnover £5.6m, Balance Sheet £2.8m, Employees 50). Do you think the cut-off could be raised to permit all companies defined as medium-sized (Turnover £22.8m, Balance Sheet £11.4m, Employees 250) under the Companies Act to use the FRSSE without any additions to the FRSSE? If not, can you identify an intermediate level for the cut-off, and what would it be?***

No response given as not relevant to our constituents.

***Q27 If you consider that the upper limit of the FRSSE could not be raised without amendment, what additional topics would the FRSSE need to cover if it was extended to include medium-sized entities, and why?***

No response given as not relevant to our constituents.

If you would like to discuss any of these issues, we would be happy to attend a meeting.

Yours sincerely,

Tim Ward
Chief Executive

**APPENDIX A**

## THE QUOTED COMPANIES ALLIANCE FINANCIAL REPORTING COMMITTEE

| Name | | Organisation |
|---|---|---|
| Anthony Carey (Chairman) | - | Mazars LLP |
| Anthony Appleton | - | PKF LLP |
| Peter Chidgey | - | BDO LLP |
| Sarah Cox | - | Ernst & Young LLP |
| Ian Davies | - | Victoria plc |
| Jonathan Ford | - | PricewaterhouseCoopers LLP |
| David Gray | - | DHG Management |
| Kern Roberts | - | Smith & Williamson |
| Chris Smith | - | Grant Thornton LLP |
| Ian Smith | - | Deloitte LLP |
| Matthew Stallabrass | - | Crowe Clark Whitehill LLP |
| Paul Watts/Bill Farren | - | Baker Tilly |
| Nick Winters/James Lole | - | RSM Tenon Group PLC |
| Colin Wright | - | UHY Hacker Young |
| Tim Ward | - | The Quoted Companies Alliance |
| Kate Jalbert | - | The Quoted Companies Alliance |

## THE QUOTED COMPANIES ALLIANCE (QCA)

A not-for-profit organisation funded by its membership, the QCA represents the interests of small and mid-cap quoted companies, their advisors and investors. It was founded in 1992, originally known as CISCO.

The QCA is governed by an elected Executive Committee, and undertakes its work through a number of highly focussed, multi-disciplinary committees and working groups of members who concentrate on specific areas of concern, in particular:

- taxation
- legislation affecting small and mid-cap quoted companies
- corporate governance
- employee share schemes
- trading, settlement and custody of shares
- structure and regulation of stock markets for small and mid-cap quoted companies;
- political liaison – briefing and influencing Westminster and Whitehall, the City and Brussels
- accounting standards proposals from various standard-setters

The QCA is a founder member of EuropeanIssuers, which represents quoted companies in fourteen European countries.

### QCA's Aims and Objectives

The QCA works for small and mid-cap quoted companies in the United Kingdom and Europe to promote and maintain vibrant, healthy and liquid capital markets. Its principal objectives are:

*Lobbying* the Government, Brussels and other regulators to reduce the costing and time consuming burden of regulation, which falls disproportionately on smaller quoted companies

*Promoting* the smaller quoted company sector and taking steps to increase investor interest and improve shareholder liquidity for companies in it.

*Educating* companies in the sector about best practice in areas such as corporate governance and investor relations.

*Providing a forum* for small and mid-cap quoted company directors to network and discuss solutions to topical issues with their peer group, sector professionals and influential City figures.

Small and mid-cap quoted companies' contribute considerably to the UK economy:

- There are approximately 2,000 small and mid-cap quoted companies
- They represent around 85% of all quoted companies in the UK
- They employ approximately 1 million people, representing around 4% of total private sector employment
- Every 5% growth in the small and mid-cap quoted company sector could reduce UK unemployment by a further 50,000
- They generate:
  - corporation tax payable of £560 million per annum
  - income tax paid of £3 billion per annum
  - social security paid (employers' NIC) of £3 billion per annum
  - employees' national insurance contribution paid of £2 billion per annum

The tax figures exclude business rates, VAT and other indirect taxes.

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# The QCA Financial Reporting Committee's Corporate Reporting Charter

## » The Quoted Companies Alliance is committed to working with boards, investors, regulators and standard-setters to promoting high quality corporate reporting by quoted companies, especially smaller quoted companies.

We will encourage the boards of quoted companies to be aware of the importance of high quality reporting in order that the market can have confidence in their businesses and in the information provided by companies generally. In order to undertake our work effectively, we will work with investors to better understand their information needs. We will also encourage standard-setters, regulators and others to set standards and other requirements that meet the genuine needs of investors in a practical way.

## » We seek to foster a culture of continuous improvement in corporate reporting.

We will encourage companies to keep their corporate reporting under regular review and to seek ways of responding to changing market needs. Information provided should be understandable, avoid unnecessary complexity, be presented in a timely fashion and in a format that makes use of modern technology where appropriate. We will similarly encourage regulators and standard-setters to remain responsive to marketplace changes and to provide information to preparers on good practice and on reporting issues which companies generally need to address. Standard-setters should also take a strategic rather than a piecemeal approach to their work and should periodically seek to eliminate requirements which have not been found to provide useful information.

## » We believe the concept of stewardship lies at the heart of good corporate reporting.

Directors are responsible to the shareholders for the long-term success of their businesses and this will have a bearing both on what they are expected to report on and the most suitable method of measurement in financial statements. It is likely to have implications, for example, for the circumstances in which fair values are used and for what is considered to be the most appropriate means of measuring fair value in particular situations.

## » Corporate reporting requirements should be subject to robust cost-benefit tests.

Standard-setters need to carefully assess the costs compared to the benefits of introducing requirements and to avoid unintended consequences wherever possible. To do this, they need to be conscious of the risks of a 'one-size-fits-all' approach since quoted companies encompass both global companies with a market valuation of tens of billions of pounds and smaller quoted

companies with one of a relatively few million pounds. Moreover, there should be a clear and public consensus between boards, investors, standard-setters, regulators and auditors on how materiality is to be applied in practice by companies when preparing their financial statements. A proportionate approach to corporate reporting that focuses on significant disclosures and avoids clutter in the financial statements with immaterial disclosures will both improve the quality of corporate reporting and reduce the costs of providing relevant information.

## » We press for accounting standards which properly reflect economic reality when implemented.

Standards when applied, as well as when written, should focus on principles and not rules, enabling appropriate judgement to be exercised, and in their drafting should take account of practical concerns raised when they are being prepared. In measurement terms, a theoretically optimum solution may turn out to be sub-optimal if, for example, the assumptions of active markets are not met in practice. A mission to reflect economic reality also calls for post-implementation reviews of issues arising. Furthermore, investors may well wish to distinguish between those profits that have between realised in cash and those that have not. Moreover, how best to reflect economic reality may be impacted by the time horizon over which performance is being measured. Further work on what is meant by, and how best to capture, economic reality in financial statements would be helpful. There should be a pre-eminent emphasis on economic reality when standard-setters agree on convergence programmes.

## » Standard-setters should be in close touch with their marketplace.

In a fast-changing modern market economy, if standards are to reflect economic reality and to be practical, the standard-setters need to be fully in touch with their marketplace. Standard-setters as a team should have substantial current or recent practical experience of operating in the marketplace as a user, preparer or adviser. They should also be drawn from a broad range of backgrounds, including those related to smaller quoted companies as well as to global corporations.

## » We emphasise the importance of good narrative reporting as an integral part of corporate reporting.

Whilst the focus on narrative reporting is increasing, it has traditionally tended to be the 'Cinderella' of the corporate reporting model. To enable the development of a business to be seen in its proper context, it is essential that high quality information be provided on its strategy, its key risks and how they are being managed, the KPIs used to manage the business, current performance and future prospects, and its corporate governance.