



Mr. Klaus-Heiner Lehne
Chair of the Committee on Legal Affairs
European Parliament
Bât. Altiero Spinelli – 10E205
Rue Wiertz 60
B - 1047 BRUSSELS

cc: please refer to the end of the letter

5 April 2013

Ref.: CRPG/AKI/TSI/IDS

Dear Mr. Lehne,

RE: Main matters of the accountancy profession on the EC Proposals for the recast of the 4th and 7th Accounting Directives

FEE has been following closely the debate on the EC Proposals for the recast of the 4th and 7th Accounting Directives (“the EC Proposals”) and expressed its views in three public comment letters¹ and in a policy statement² on relevant matters since the issuance of the EC Proposals on 25 October 2011.

Since the European Council and the European Parliament together with the European Commission have engaged in the trilogue, FEE would like to draw your attention to some of the main matters that would help adopting a useful Accounting Directive for Europe. We hope this will further inform the debate and help close the gap between the differences of views in the European Parliament and the Council. FEE considers that those involved in the decision should be in a position to make the best choice for Europe at what is a critical moment for the European economy and the internal market.

Simplification and reduction of administrative burdens

Our comments below on the EC Proposals are made on the backdrop of our firm belief that accounting and auditing are not “administrative burdens”. They are essential tools to enable managers to manage, investors to invest and enterprises to trade, grow and create wealth and employment; accounting and auditing also have a public interest dimension by contributing to improving the functioning of markets and enhancing corporate governance, transparency and stability.

¹ See: [FEE comment letter, 23 May 2012](#) and [FEE comment letter, 23 April 2012](#)

² See: [Policy Statement on main issues of the accountancy profession on the EC proposals for the recast of the 4th and 7th Accounting Directive, November 2012](#)

Main matters related to accounting and financial reporting

General accounting principles should be applicable to all aspects of financial reporting

As FEE supports a principle-based Accounting Directive, it welcomes the introduction of high level general accounting and reporting principles, such as the true and fair view, as well as materiality, substance over form and prudence. They are instrumental to fulfil the primary objective of reporting to provide relevant and useful information to users. Therefore, these interrelated principles should be generally applicable to all aspects of accounting and financial reporting including recognition, measurement, presentation and disclosure.

FEE questions the real benefits of a fully prescribed reporting regime for small companies

The EC Proposals replace the Member State reporting regime that currently exists for disclosures or notes to the financial statement for small companies with a maximum harmonisation approach. This would mean that Member States would no longer be allowed to require the presentation of any additional information for small companies, whether or not the Member State considers that such additional information would be needed to fulfil the general principle of presenting a true and fair view of the financial position and performance of a small company. A fully prescribed reporting regime for small entities seems to contradict this general provision of the EC Proposals on the true and fair view.

Given the current economic climate, it is vital that businesses are able to access capital, an issue of particular importance for SMEs. In this respect, transparent financial information is crucial. Reduction of necessary disclosures will likely reduce the quality and the usefulness of the financial information available to users, while it will not result in any significant cost reductions, since companies will still be required to keep detailed accounting records. Instead, it will mean that relevant information is not disclosed and stakeholders may lose confidence in whether all relevant disclosures have really been made.

FEE noted that the final report of the European Parliament Legal Affairs Committee (JURI Committee) of 25 September 2012 included further reductions to the set of disclosures prescribed in the EC proposals. It proposed to remove the disclosure requirements of off-balance sheet transactions for small companies, related party transactions for small and medium-sized companies and post balance sheet events for any type of companies.

FEE finds this very unfortunate and therefore urges all parties involved in the trilogue to maintain the mandatory disclosures on off-balance sheet and related party transactions as well as post balance sheet events for small companies. This is a critical element of transparency and does not create administrative burdens.

Furthermore, FEE supports giving the Member States an option to require further disclosures for small companies that they deem necessary under their local and particular circumstances to comply with the overarching principle of presenting a true and fair view of the financial position and performance of all reporting entities, including small ones. This is particularly important for the many EU Member States where virtually all companies are small entities. In such Member States, the premise on which the EC

Proposals are built, with a more elaborate disclosure regime for medium-sized and an even more complete one for large entities is irrelevant.

Fair value accounting should be permitted as a Member State option

While the EC Proposals intended to keep a Member State option to permit or require fair value accounting as an alternative measurement base for specific assets, the JURI Committee in its final report of 25 September 2012 proposed to prohibit this practice by the deletion of the option from Article 7.

In this respect, it is important to note that since the 2005 IAS Regulation requiring the use of IFRS for consolidated accounts of publicly-traded companies came into force, Member States have also been able to permit or require the application of IFRS for annual accounts (financial statements) of publicly-traded companies and of non publicly-traded companies.³

This means that Member States can already permit or require for all companies, which fall under the scope of the 4th and 7th Directives, the use of the full set of IFRS which permits fair value accounting as a measurement base for certain relevant account balances.

In order to increase the usefulness of information in the financial statements, FEE urges all parties involved in the trilogue discussions to retain a Member State option permitting or requiring fair value accounting for certain relevant account balances. A possible blanket prohibition of fair value accounting would have significant negative implications for transparency and for those Member States that have already adopted this approach.

Make the use of IFRS for SMEs possible

From a European perspective, FEE regrets that the EC Proposals do not seize the opportunity to allow EU Member States to make their own decision to opt to use IFRS for SMEs or not. This would be of help to certain jurisdictions, in particular Member States with limited standard-setting capacities. It would be unfortunate that differences between the EC Proposals and the current IFRS for SMEs for the accounting treatment of relatively minor matters may impede the use of this standard in EU Member States which would like to use it⁴.

We find it encouraging to see that there have been significant efforts made during the trilogue to remove the existing obstacles. In particular, we refer to the Danish Presidency compromise text of 19 June 2012 introducing a Member State option to determine the write-off period for goodwill from 5 to 10 years, which would remove one of the two obstacles impeding Member States to use IFRS for SMEs for national accounting and reporting purposes.

FEE believes that also the IASB should take action and address the last remaining impediment to make the use of IFRS for SMEs possible for Member States.

³ Reference is made to the EC survey results on the implementation of the IAS Regulation (1606/2002) in the EU and EEA for more details on countries using the option to permit or require IFRS for annual accounts of publicly-traded companies and of non publicly-traded companies:
http://ec.europa.eu/internal_market/accounting/docs/ias/ias-use-of-options_en.pdf.

⁴ Differences are in the areas of presentation of unpaid subscribed share capital and the amortisation periods for goodwill whose expected useful life cannot be reliably estimated.

FEE urges all the parties involved in the trilogue to permit Member States to opt for the use of IFRS for SMEs for national reporting purpose if they so desire. The Accounting Directive should not include obstacles which go against this. The Presidency compromise text of 19 June 2012 would be a good approach. FEE wrote to the IASB and encouraged it to change its approach to unpaid subscribed share capital.

Permit merger accounting as a simplification measure

The provisions allowing merger accounting are removed from the EC Proposals. This is likely to be of concern to certain companies as merger accounting is widely used in practice which often better reflects the economic substance of the underlying transactions for certain types of business combination, e.g. transactions under common control or a group restructuring. This accounting option also simplifies accounting and thus reduces costs for preparers.

Therefore, FEE encourages the parties involved in the trilogue discussions to reintroduce the provision allowing the Member States to permit the use of merger accounting.

Requiring cash flow statements would benefit enterprises and stakeholders

It is a missed opportunity not to have prescribed the preparation and presentation of a cash flow statement for certain types of companies in the EC Proposals.

The cash flow statement is an essential tool to provide relevant information about the cash generating capacity of a company and to assist in making the connection between the balance sheet and profit and loss account. It gives, in combination with the profit and loss account, a more rounded and complete view of the performance and cash generation capacity of a company, which is particularly important in periods of instability.

Therefore, FEE encourages the European Parliament as well as the Council and European Commission to consider the mandatory inclusion in the annual financial statements of a cash flow statement for large companies and to introduce a Member State option to require it for medium-sized companies.

The auditor's involvement with financial statements and the management report

The auditor's view as to the entity's assumption that it is a going concern

The European Commission proposals to reform the statutory audit⁵ include a proposal in Article 22, 2 (l) that the auditor is required to provide a statement on [management's assessment] and disclosure of the audited entity's ability to meet its obligation in the foreseeable future and therefore continue as a going concern.

However, currently, there is no Europe-wide requirement for the entity to explicitly include comments on its going concern assumptions in the financial statements. With the growing interest in additional information on going concern assessments from investors, entities should be required to provide more information on the assumptions and other information they have used to support management's assertion that the entity would be able to continue its activities in the foreseeable future, currently normally for a period of at least one year. This is especially important in situations where there may be concerns about the impact of future events.

⁵ See: http://ec.europa.eu/internal_market/auditing/docs/reform/regulation_en.pdf

FEE encourages all parties involved in the trilogue to consider the inclusion of such requirement in the Accounting Directives, or to at least include a clearer statement that the accounting policies note should include a confirmation by management that the accounts have been prepared on a going concern basis or an explanation why that basis is not appropriate.

The auditor's involvement with the management report

The accountancy profession and in particular auditors are ready to meet the growing needs of users of financial statements and make our audit reports more informative, comprehensive and exhaustive.

Therefore, except for a technical wording change as indicated below, we support the amendments proposed by the JURI Committee in its final report of 25 September 2012 on the auditor's opinion on the management report. It proposes to retain subparagraph 2 of Article 34.1 in the EC Proposals with additions which would result in the following wording:

"The statutory auditor shall also report concerning ~~express an opinion on:~~

- a) the consistency of the management report with the financial statements for the same financial year and*
- b) whether the management report has been prepared in accordance with the applicable legal requirements, and*
- c) whether according to the auditor's knowledge and understanding of the undertaking and its environment obtained during the course of the audit, the management report as a whole suitably presents the undertaking's position, the opportunities and principal risks and uncertainties of its likely future development."*

In addition, to ensure internal consistency between the articles of the Accounting Directive, Article 20 *Contents of the management report* and the related recital 15 would also require some rewording. Furthermore, the European Commission proposals on statutory audit would also need to be brought in line with the Accounting Directives in respect of auditor's involvement with the management report.

FEE recommends taking into account the above mentioned changes while debating the content of the audit opinion on the management report during the trilogue discussions.

Swift finalisation of the debate on Country-by-Country reporting

FEE has supported the idea of improving transparency and accountability in resource-rich emerging economies while warning against the risk of obscuring financial statements with Country by Country information rather than including such information in a separate report. We appreciate that the political debate is no longer only centred on these matters but has started to take a broader perspective on the EC Proposals and is now focused on the development of an accounting framework *fit for purpose* for the European economy.

Therefore, FEE encourages all parties involved in the trilogue discussion to close the gap between the different views on Country-by-Country reporting to allow for a successful finalisation of the Accounting Directive as a whole. This Directive will underpin an accounting framework which is likely to remain applicable in Europe for a considerable time in the future, therefore the decisions the Institutions are about to take are critically important.

We hope our comments, based on the experience and expertise of European accountants, may be of help to the Members of the European Parliament, European Council and European Commission when considering these important matters. Should you wish to discuss any of these points in more details, please contact Hilde Blomme, FEE Deputy Chief Executive, on +32 2 285 40 77 or via email at hilde.blomme@fee.

Sincerely,



André Killesse
President



Olivier Boutellis-Taft
Chief Executive

cc:

European Parliament

Mr. Wolf Klinz, Rapporteur for opinion on the Accounting Directive
Ms. Franziska Katharina Brantner, Rapporteur for opinion on the Accounting and Transparency Directive
Ms. Fiona Hall, Rapporteur for opinion on the Accounting and Transparency Directive
Mr. Helmut Scholz, Rapporteur for opinion on the Accounting and Transparency Directive
Ms. Arlene McCarthy, Rapporteur for the Transparency Directive
Ms. Sirpa Pietikäinen, Rapporteur for opinion on the Transparency Directive
Mr. Elmar Brok, Chair of AFET
Ms. Eva Joly, Chair of DEVE
Mr. Vital Moreira, Chair of INTA
Mr. Sajjad Karim, Rapporteur on the Audit Reform Directive and Regulation

Ms. Sharon Bowles, Chair of ECON
Ms. Amalia Sartori, Chair of ITRE
Mr. Malcolm Harbour, Chair of IMCO

Irish Presidency of the Council of the European Union

Ms. Breda Power, Department of Jobs, Enterprise & Innovation
Mr. Patrick Houlihan, Chair of the Council Working Party on Company Law

Competitiveness Council

Mr. Philip Kelly, Assistant Secretary, EU Affairs
Mr. Thomas Murray, Principal Officer, EU issues, Competitiveness Council
Mr. Aidan Hodson, Principal Officer, Research policy, Science and Technology
Mr. John Kinnane, Assistant Principal, Procurement Policy
Ms. Róisín McCann, Press Officer

European Commission

Mr. Didier Millerot, Head of Accounting and financial reporting Unit, DG Internal Market and Service
Ms. Anne-Françoise Melot, Deputy Head of Accounting and financial reporting Unit, DG Internal Market and Service