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Our ref: ICAEW Rep 168/13

Your ref: CBCR Guidance Consultation

Ali Uppal
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Financial Services Group
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Via email: CBCRconsultation@hmtreasury.gsi.gov.uk

Dear Ali,

Capital Requirements (country-by-country reporting) Regulations 2013: draft guidance

ICAEW is pleased to respond to your request for comments on *Capital Requirements (country-by-country reporting) Regulations 2013: draft guidance*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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ICAEW REPRESENTATION

CAPITAL REQUIREMENTS (COUNTRY-BY-COUNTRY REPORTING) REGULATIONS 2013: GUIDANCE

Memorandum of comment submitted in November 2013 by ICAEW, in response to HM Treasury consultation paper Capital Requirements (country-by-country reporting) Regulations 2013: draft guidance published in November 2013.

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation paper *Capital Requirements (country-by-country reporting) Regulations 2013: draft guidance* published by HM Treasury (HMT) on 19 November 2013, a copy of which is available from this [link](#).

WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
4. The Financial Services Faculty was established in 2007 to become a world class centre for thought leadership on issues facing the financial services industry acting free from vested interest. It draws together professionals from across the financial services sector and from the 25,000 ICAEW members specialising in the sector and provides a range of services and a monthly magazine FS Focus.

MAJOR POINTS

5. We would like to thank the HMT team for reflecting much of the feedback received on the earlier consultation on country-by-country reporting and for working to produce the draft guidance to such a short timeframe. We recognise that the guidance can continue to evolve following its initial publication and codification of the statutory instrument. We would welcome the opportunity to work with the HMT team on improving the guidance to take into account the experience of the interim reporters and continued thinking which will take place following the close of the short consultation period dictated by the European Union.
6. We must emphasise at the outset that it is very difficult to provide adequate or meaningful feedback in a consultation period of one week. Our response highlights what we consider to be the most fundamental areas of the guidance and statutory instrument which require resolution in order to be practical documents for the institutions required to report on the December 2013 year end. It does not purport to capture all issues which may be found to have an impact on reporting going forward.
7. We have significant concerns that, in its current form, the guidance on how institutions are expected to allocate turnover and profit and loss before tax is insufficient as it will allow wide scope for interpretation. For example basing location only on that of the registered office without regard to where the activities are undertaken, may result in misleading disclosures. It is also not clear that the tax paid will relate to the country to which the entity has been allocated. In the absence of clarity the comparability goals of the disclosure and guidance are unlikely to be met.
8. There are significant political and public expectations that the most appropriate and accurate information is presented under the country-by-country reporting requirements. Without sufficient, clearly articulated guidance, we are concerned that disclosures may fail to meet these expectations. Ineffective execution of the country-by-country reporting requirements will reflect badly on not only the financial services industry, which is working hard to restore its

reputation, but also politicians if they provide legislation without clearly articulating what will meet their expectations.

9. As noted above we would welcome the opportunity to work with your team to help ensure that guidance is prepared that meets the needs of its users, and facilitates disclosure that is fit for purpose, understandable and cost-effective to prepare and assure. It is vital that this is done before the requirement for public disclosure is implemented. We would be keen to engage with the HMT team early in the second quarter of 2014 to consider the most effective way to produce such guidance.
10. We note that the period set out by the European Commission for their analysis and decision making as to whether the requirements set out in 3(4) (d) (e) and (f) of the statutory instrument be made publicly available is short and will include only the first reporting cycle of a limited number of institutions. We do not feel this will allow them adequate information on which to base a decision, given the magnitude of the interest in this area. We urge the Government should make these concerns known to the European Commission and call for the pursuit of a meaningful analysis of country-by-country reporting over at least two years. This will enable the Commission to make an informed decision about public disclosure, rather than the current expedited timetable for review.
11. We are aware that country-by-country reporting requirements may be extended, both in terms of the scale of disclosures and the types of business covered. We strongly believe that disclosure required by the directives should be subject to due process to ensure that users' reasonable information needs can be met as cost effectively as possible. We encourage HMT to work with the Department for Business, Innovation and Skills in both developing this legislation and in ensuring that views of users, preparers, and auditors are fully taken into account in the development of any further country-by-country disclosures.
12. As expressed in our previous response, we support the tax transparency goals pursued by this initiative, but feel that the requirements for individual entities or groups which operate and pay tax solely within one country are onerous. We urge HMT to work with the Financial Conduct Authority to ensure that smaller firms are aware of their responsibilities under the law for production of this information.

RESPONSES TO SPECIFIC POINTS

Statutory Instrument text

13. Given the short timetable to implementation and transitional nature of the first year of disclosure, we would support HMT in encouraging the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) to take a pragmatic and reasonable approach to enforcing the regulations. This would allow institutions to work with the regulators and government to further understand the information requirements, as well as develop the most effective ways of reporting.
14. With regard to paragraph 6 on prior disclosure: prevention of duplication, where UK companies are able to rely on reporting by a parent (in the same jurisdiction or in another member state), we feel this could be enhanced by stating that the order of reporting is not relevant. In practice this would mean that the UK company can publish its annual report before the parent rather than after and it is still exempt from reporting, as long as the relevant references to where and when the information will be available are made.
15. The wording of paragraph 3(3) should be clarified with regard to year ends contiguous to the date of disclosure and in the quarter immediately preceding the date of disclosure so as not to imply unduly onerous requirements. There also may be a disproportionate burden on March year end preparers during the interim disclosure period.

16. We suggest changing the wording in paragraph 3(7) to 'annual report' rather than 'annual financial statement'.
17. Regulation 3(8) refers to standards under Directive 2006/43/EC. No international standards have yet been approved for use by the EC under Article 26 of this Directive, and we suggest that it might be better to refer to standards issued by the FRC and/or IAASB.
18. Regulation 5 'group disclosure' could specify that the disclosure required is limited to EU groups only and can either be made by the top parent company and/or by the regulated entity and subsidiaries (sub-group). To make this clearer the word "EU" could be inserted into both the regulation and to the accompanying draft guidance.
19. At the time of writing this response we are aware that the European Commission has begun to communicate with the relevant institutions regarding their submission of reporting on a private basis as noted in the explanatory note, and would expect Her Majesty's Revenue and Customs (HMRC) to communicate with institutions as promptly as possible following the UK legislation.

Draft guidance text

20. The guidance in paragraph 2.9 should be clarified. We are concerned that the guidance could be unduly widely interpreted, in particular for those companies that are incorporated in one jurisdiction, but carry out their business (and are resident for tax purposes) in the UK or other EU member states. It might for example mean that the CBCR information (turnover, profits, taxes) is disclosed in the jurisdiction where it is incorporated, while the preference (reflecting the substance of the arrangements) would be to disclose it to the jurisdiction where the business is carried out and where the taxes are paid. It would therefore be preferable for the guidance to be less specific and to set out a principle to accommodate as many fact patterns as possible.
21. We note that International Financial Reporting Standards (IFRS) take a different approach to segmental disclosure; requiring information to be presented based on how information is reported to the chief operating decision maker, and explained if this does not fit with how it is disclosed in the primary financial statements. This allows entities to present the geographical substance of their business, not necessarily based on where they are legally incorporated. We note that where there is not an alignment in the location of incorporation and economic activity, an explanatory narrative will certainly be required.
22. We believe that some institutions may require further guidance as to whether inclusion within the statutory audit or a separate assurance engagement is most appropriate to meet their requirements. Inclusion in the annual report can be confusing, as it is not based on an investor driven need. Clear guidance in this area would help to make sure that the institutions (likely to be smaller institutions) access the most effective and efficient services to meet their needs, and commission an engagement which will fulfil their regulatory requirement. The distinction should also be borne in mind by the auditor or assurance practitioner as the different engagements will have different risk management considerations.
23. We suggest the removal of 'International Standards on Review Engagements' from paragraph 2.15. Such engagements offer a limited, as opposed to a reasonable, level of assurance and are not capable of offering a similar level of comfort to a statutory audit as required by paragraph 2.16. We would not preclude the future use of limited assurance on such disclosure as reporting as good practice emerges and user expectations of this and other such disclosure develop further,
24. Finally, we suggest that paragraph 2.17 clarifies that the materiality should be appropriate for "country-by-country reporting *taken as a whole*." This would clarify that it was not necessary for an individual materiality to be used for each country, which could lead to a disproportionate amount of work.

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