

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Fourth Delegated Legislation Committee

DRAFT INTERNATIONAL ACCOUNTING
STANDARDS (DELEGATION OF FUNCTIONS)
(EU EXIT) REGULATIONS 2021

Thursday 15 April 2021

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The Committee consisted of the following Members:

Chair: MRS MARIA MILLER

Abrahams, Debbie (<i>Oldham East and Saddleworth</i>) (Lab)	† Mann, Scott (<i>North Cornwall</i>) (Con)
Caulfield, Maria (<i>Lewes</i>) (Con)	Morris, James (<i>Lord Commissioner of Her Majesty's</i> <i>Treasury</i>)
† Davies, David T. C. (<i>Parliamentary Under-Secretary</i> <i>of State for Wales</i>)	Pursglove, Tom (<i>Corby</i>) (Con)
Duguid, David (<i>Parliamentary Under-Secretary of</i> <i>State for Scotland</i>)	† Scully, Paul (<i>Parliamentary Under-Secretary of</i> <i>State for Business, Energy and Industrial Strategy</i>)
† Fletcher, Colleen (<i>Coventry North East</i>) (Lab)	Thomson, Richard (<i>Gordon</i>) (SNP)
Foy, Mary Kelly (<i>City of Durham</i>) (Lab)	Throup, Maggie (<i>Lord Commissioner of Her</i> <i>Majesty's Treasury</i>)
Gardiner, Barry (<i>Brent North</i>) (Lab)	† Whitehead, Dr Alan (<i>Southampton, Test</i>) (Lab)
Gideon, Jo (<i>Stoke-on-Trent Central</i>) (Con)	
Harris, Rebecca (<i>Lord Commissioner of Her Majesty's</i> <i>Treasury</i>)	Chloe Freeman, <i>Committee Clerk</i>
Jones, Darren (<i>Bristol North West</i>) (Lab)	† attended the Committee

Fourth Delegated Legislation Committee

Thursday 15 April 2021

[MRS MARIA MILLER *in the Chair*]

Draft International Accounting Standards (Delegation Of Functions) (EU Exit) Regulations 2021

11.30 am

The Parliamentary Under-Secretary of State for Business, Energy and Industrial Strategy (Paul Scully): I beg to move,

That the Committee has considered the draft International Accounting Standards (Delegation of Functions) (EU Exit) Regulations 2021.

It is a pleasure to serve under your chairmanship, Mrs Miller. The regulations, laid before the House on 1 February 2021, follow on from the International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019—the principal regulations—which aimed to address failures of retained EU law to operate effectively in the field of accounts and reports from UK corporate bodies.

International financial reporting standards are a set of international accounting standards used in more than 125 countries across the world, including Australia, Canada and in the EU. Their widespread use provides consistent and comparable financial reporting that facilitates transparency, accountability and investment across borders. In 2005, the UK mandated the use of IFRS as endorsed and adopted by the EU for all publicly traded companies when preparing their consolidated accounts. The UK is the largest single user of the standards: we estimate that 15,000 UK companies use them, including those that do so voluntarily.

In preparation for our departure from the EU, the principal regulations transferred all existing EU-adopted IFRS into UK law to form UK-adopted international accounting standards. They also provided the Secretary of State with the power to adopt new IFRS for use in the UK after the transition period. That action meant that the UK was able to adopt crucial amendments to IFRS immediately after the transition period, including those relating to the ongoing interest rate benchmark reform. Despite the framework being only a few days old, the UK adopted the amendments ahead of the EU.

That was, however, intended only as a temporary solution. The regulations delegate the power to adopt IFRS for use in the UK from the Secretary of State to the UK Endorsement Board. The board will provide the specialist expertise and dedicated resource to undertake two key functions: to make the final decision on whether all new standards, amendments and interpretations should be adopted for use in the UK; and to influence the development of IFRS by the International Accounting Standards Board.

I will quickly explain how the endorsement board will undertake those functions. To adopt a standard, the board will need to be satisfied that the standard meets

the statutory criteria. The criteria are: its application is likely to be conducive to the UK's long-term public good; the standard meets the criteria of understandability, relevance and comparability; and its application would not be contrary to the principle that accounts provide a true and fair view. The board's activities will be undertaken in line with the four guiding principles of accountability, independence, transparency and thought leadership.

The board will be required to consult publicly before taking a decision and will be independent in that technical decision making. In addition, the board will have a significant role in influencing the development of new standards, which will be delivered through proactive engagement with the IASB at all stages of the development of a standard, together with building and maintaining the UK's international reputation as a world leader in accounting excellence. In that way, the endorsement board will work to ensure that IFRS remain suitable for use in the UK.

The UK Endorsement Board is comprised of a group of experts with backgrounds and experience across different sectors with a strong interest in the quality of financial reporting in the UK. The board will be led by Pauline Wallace, who was appointed as interim chair in September 2020. Pauline has been instrumental in completing the establishment of the board, and I extend my thanks to her for her tireless work in bringing the board to this point of readiness. The remaining 10 members of the board were appointed following an open and transparent recruitment process. They comprise representatives from preparers of accounts, investors, academics and members of accounting firms. The board is an independent, unincorporated association with its operations facilitated by a subsidiary of the Financial Reporting Council.

The FRC will provide support in the areas of human resources, finance and IT equipment under the terms of a service level agreement. That will ensure that the board will have the necessary resources to undertake its functions without compromising the independence of its technical decision making. I am grateful to the FRC for its support for the project. The endorsement board will be funded by the FRC's levy on preparers of accounts and audit firms, which means that the cost of the board will be borne by those who benefit most from the use of IFRS. Ongoing costs are expected to amount to about £2.9 million annually.

I have already set out that the endorsement board will be independent in its decision making. However, that does not mean that it is beyond active oversight and public scrutiny. The endorsement board will be required to report to the Secretary of State on the carrying out of its statutory functions on at least an annual basis. This report will be laid in Parliament. Meetings will be held in public, discussion papers will be published, and the board must publish decisions reached within 10 working days. The inaugural board meeting took place on 26 March, and is available to view on the board's website. The board will also report to the FRC on its governance and due process in a publicly available document.

In conclusion, Mrs Miller, I hope that the Committee will recognise that the instrument is in the UK's long-term interest, and agree that now is the time for the UK Endorsement Board to be given the functions envisaged by the principal regulations. I commend this instrument to the Committee.

11.35 am

Dr Alan Whitehead (Southampton, Test) (Lab): I ought to indicate immediately that we do not intend to oppose this regulation. Indeed, we see the need to ensure that the international standards, which have now been put in place across the world, are properly placed into a UK context, particularly given the UK withdrawal from the EU. There is also a context in terms of an independent body that can bring those standards forward and into the mainstream of UK accounting life, in good order, with confidence behind it so that the UK can be seen to be playing its part in the international structure that is now the norm for those accounting standards.

However, I have a couple of questions for the Minister about the process by which this has been set up. I thank him for going substantially beyond the explanatory notes in his introductory comments this morning; he has fleshed out one or two things that I wanted to focus on.

My concerns are that the SI itself, by way of a preamble declaration, states that:

“It appears to the Secretary of State that—

(a) the UK Endorsement Board is able and willing to exercise the functions transferred by regulation 2 of these Regulations, and

(b) that body has arrangements in place”,

and so on. I suppose the Secretary of State would say that, since it was the Secretary of State who very recently indeed created the UK Endorsement Board, as the Minister has set out. It is difficult to see how the Secretary of State could know that this brand new board is indeed

“able and willing to exercise the functions”,

as it has no track record and it has not undertaken any significant activities.

The only activity of the UK Endorsement Board so far has been to bring itself into being, and that has been done by a rather curious route. First, the chairman was appointed—by the Secretary of State, I assume—and the chairman then essentially constructed her own board. That is not absolutely normal practice: the board usually elects the chairman, rather than the chairman electing the board, but perhaps that is a part of the process of bringing these things into being.

Then we have the question of the independence and accountability of the board; I wonder to whom exactly the board is accountable. It is barely accountable to Parliament. One could say that it is perhaps rather more accountable to the accountancy profession, as most of the members of the board who have been appointed are accountants. The potential danger for the board is that, in a circular way, it reflects its own view of the profession on the profession itself. I would like reassurance from the Minister that that, in his view, will not happen as a result of the work of the endorsement board as it goes forward.

The other matter, as far as independence is concerned—I always look for it when such things happen—is how the board is funded. Has it got independent pay and rations, and can it guarantee the funding that the Minister elucidated was £2 million or so?

Paul Scully: It is £2.9 million.

Dr Whitehead: Okay, £2.9 million. How is that actually guaranteed? It turns out that it is to be sorted out and guaranteed through a subsidiary company of the FRC, which, again, is a slightly unusual procedure for guaranteeing pay and rations and organisational independence for such a body. It is especially unusual in view of the fact that the FRC is about to be abolished. It is to be replaced by the interestingly named ARGA—the Audit, Reporting and Governance Authority, which does not exist yet. We are still awaiting a paper promised for the spring of 2021. Cold weather notwithstanding, I am assured that it is now the spring of 2021, so we await the detail of what the new body is expected to do, how it will be set up and organised, at what point the FRC ceases to exist, and how the functions of the FRC will be transferred to ARGA.

There is a particularly important element: the guaranteed transfer of financial independence from that subsidiary of the FRC to, I presume, something relating to ARGA at the point when FRC ceases to exist. Can the Minister give a brief assurance that there will be no hitches and that there will not be any necessary further secondary legislation to secure the proper transfer of the financial arrangements relating to the board from the subsidiary of the FRC to a possible subsidiary of ARGA? I think he will agree that this looks a little rickety at the moment.

As I have said, the really important international regulations will be placed in the hands of a body that has only just come into existence and that is funded by a body that is just about to go out of existence. I hope the Minister can give us some assurances about the solidity and continuity that we should be able to expect from such an arrangement for the future. I am sure he will be able to satisfy us on those matters this morning.

11.44 am

Paul Scully: I am grateful for the insightful contributions to the debate.

We have discussed the fact that 15,000 UK companies apply the IFRS. That is why it is important that we get consistency of reporting and enhanced transparency for investors, which obviously brings benefit to UK capital markets.

I will cover some of the very pertinent questions that the hon. Gentleman raised. As for the UK Endorsement Board itself and its make-up, we appointed Pauline Wallace without a public appointment process. That was necessary to facilitate the establishment of the endorsement board in time for it to consider IFRS 17, the major new insurance standard. That met the exceptional circumstances, referred to in the board’s terms of reference, in which an interim appointment can be made. However, we will advertise for a permanent chair later this year, following the public appointments process, which is important.

The future UK Endorsement Board chair and members will be appointed following an open and transparent recruitment process, to demonstrate the independence and robustness of the board in the way that has been described. The chairman will be appointed by the Secretary of State and the board members will be appointed by the chair, upon the approval of the Secretary of State.

[Paul Scully]

As for how the board will be shown to be in the public interest, clearly this goes right to the heart of how and why the board is established. The statutory instrument transfers the responsibilities under the principal regulations to the UK Endorsement Board, but that includes the requirement that the standard must be in the long-term public good. That means that public interest will be absolutely at the heart of the endorsement board's activities, which is underpinned by the terms of reference.

Regarding funding, I talked about the fact that it will come indirectly from a levy on the people who most benefit from these standards—the £2.9 million that is expected from 2021 to 2022. It will be funded from the Financial Reporting Council levy, which puts the cost directly on those who benefit most from the IFRS. That spending represents value for money, because it allows the UK to influence directly the international standard setters and ensure that the development of the standards takes into consideration any UK public good issues before being finalised.

We worked closely with the FRC during the development of the UK Endorsement Board and we are confident that it has the capacity to perform its oversight role. However, it was important that the creation of the endorsement board was not delayed while we were waiting for ARGA to be formed in the first place. When

ARGA is functioning, it will take over the FRC's responsibilities in relation to the oversight of the UK Endorsement Board's governance and due process. We recognise that that transition needs to be smooth, to give certainty to businesses that these standards will be maintained and that the levy is maintained to fund the board satisfactorily.

Clearly, there is an ambitious remit, but I am confident that the endorsement board will meet the challenges and make a valuable contribution to financial reporting, both in the UK and further afield. We set high standards for bodies with decision-making powers, and in the endorsement board the Government have recognised the need to balance independent decision making with accountability and transparency, to ensure that we can give the certainty that the hon. Member for Southampton, Test is rightly seeking. Members of this Committee and all other parliamentarians will have the opportunity to scrutinise on an annual basis how the board carries out its functions, which are delegated by this SI.

I thank hon. Members again for their valuable contribution and for giving their time to this debate. The UK Endorsement Board is now ready, and I hope the Committee will approve this SI.

Question put and agreed to.

11.49 am

Committee rose.