

EXPLANATORY MEMORANDUM TO
THE SUPERVISION OF ACCOUNTS AND REPORTS (PRESCRIBED BODY) ORDER
2007

2007 No. 2583

1. This explanatory memorandum has been prepared by the Department for Business, Enterprise and Regulatory Reform and is laid before Parliament by Command of Her Majesty.

2. Description

2.1 The Supervision of Accounts and Reports (Prescribed Body) Order 2007 appoints the Financial Reporting Review Panel (FRRP) to review periodic accounts of issuers of certain types of transferable securities admitted to trading on a regulated market. It is effective in respect of periodic accounts and reports relating to financial years beginning on or after 20 January 2007. It replaces the Supervision of Accounts and Reports (Prescribed Body) Order 2005¹, which gave the FRRP similar powers in respect of issuers of listed securities: but the 2005 Order will continue to apply in respect of periodic accounts and reports relating to financial years beginning before 20 January 2007.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 Article 2(2)(a) refers to section 14(2) of the Companies (Audit, Investigations and Community Enterprise) Act 2004 (CAICE Act) as amended by the Companies Act 2006 (2006 Act). This is to put beyond doubt that the continued operation of the Supervision of Accounts and Reports (Prescribed Body) Order 2005 is in respect of periodic accounts and reports to which the amended Act applies and not those to which the Act applied when the 2005 Order was made. Those periodic accounts and reports to which the unamended Act applied but the amended Act does not apply should not be subject to the 2005 Order as continued in effect by the 2007 Order, because it is not within the *vires* of the amended Act to make any provision in the 2007 Order for periodic accounts and reports to which the amended Act does not apply.

4. Legislative Background

4.1 Under section 89A of the Financial Services and Markets Act 2000 (FSMA), the Financial Services Authority (FSA) has power to make rules for the purposes of the Transparency Obligations Directive². The FSA has exercised this power to make rules implementing the provisions of the Directive requiring issuers of specified securities to produce periodic financial information. FSMA also requires the FSA (in paragraph 6 of Schedule 1) to maintain arrangements for monitoring compliance with its rules and

¹ SI 2005/715.

² Directive 2004/109/EC of the European Parliament and of the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (OJ L 390, 31 December 2004, page 38).

enforcing them. The Directive also introduces a new obligation on Member States to have a Competent Authority responsible for reviewing and monitoring this information.

4.2 Section 14 of the CAICE Act gives the Secretary of State the power to make an order appointing a body to exercise certain functions. In section 14 as originally enacted those functions were (1) keeping under review periodic accounts and reports that are produced by issuers of certain listed securities and are required to comply with any accounting requirements imposed by FSA listing rules, and (2) if it thinks fit informing the FSA of any conclusions reached by the body in relation to such accounts or reports. The 2006 Act amended the first function in section 14, and this is now keeping under review periodic accounts and reports that are produced by issuers of transferable securities and are required to comply with any accounting requirements imposed by rules under Part 6 of FSMA. Without this amendment to section 14, the functions of FRRP would not have been wide enough to enable them to act as the Competent Authority for the purpose of examining whether financial information is drawn up in accordance with the requirements of the Transparency Obligations Directive and taking appropriate measures in the case of discovered infringements (as permitted by article 24 of that Directive). A body may be appointed to carry out these functions if it has an interest in, and has satisfactory procedures directed to, monitoring compliance by issuers of transferable securities with accounting requirements imposed by rules under Part 6 of FSMA in relation to periodic accounts and reports.

4.3 The FRRP was appointed by the Secretary of State under section 14 of the CAICE Act by the Supervision of Accounts and Reports (Prescribed Body) Order 2005. It was appointed in respect of any issuer of listed securities which is incorporated in the UK, or which is incorporated outside the UK and has a primary listing of its equity securities (or securities convertible into such securities).

4.4 The Transparency Obligations Directive imposes requirements to produce periodic financial reports on a different but broadly wider range of issuers, including, in particular, overseas issuers of securities other than equity securities, for example bonds, and overseas issuers of securities that are admitted to trading on a regulated market, but which are not listed.

4.5 The Supervision of Accounts and Reports (Prescribed Body) Order 2007 extends the responsibilities of the FRRP to periodic accounts and reports of issuers of transferable securities admitted to trading on a regulated market that are subject to accounting requirements under the Transparency Obligations Directive, where the issuer's home state is the UK.

4.6 HM Treasury Explanatory Memorandum 24415 8062/03 COM(03)138 in respect of the Transparency Obligations Directive was submitted on 8 April 2003. The Commons European Scrutiny Committee considered it politically important and did not clear it (21st Report, Session 2002/03). Transposition Notes for the Transparency Obligations Directive are attached at Annex A.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

7.1 The FRRP is part of the Financial Reporting Council, the UK's independent regulator responsible for promoting confidence in corporate reporting and governance. It is responsible for considering whether the annual accounts of public companies and large private companies comply with the requirements of company law, including applicable accounting standards. It also keeps under review the periodic accounts and reports of certain other listed issuers.

7.2 The purpose of the Transparency Obligations Directive is to enhance transparency in EU capital markets in order to improve investor protection and market efficiency. It does this by establishing rules on periodic financial reports (i.e. annual, half yearly and quarterly) and other continuing reporting obligations, and on the disclosure of major shareholdings, for issuers whose securities are admitted to trading on a regulated market in the EU.

7.3 The FSA has responsibility under FSMA for monitoring and enforcing its rules including its rules in relation to periodic financial reporting. However, the Transparency Obligations Directive contemplates that Member States can designate a separate Competent Authority with the function of monitoring and reviewing in relation to periodic financial reporting. The FRRP will be designated in relation to periodic accounts and reports produced by the issuers specified in the Order.

7.4 The Government considers that this designation is the best approach to meeting the obligation to monitor and review. It ensures that the UK is efficient in its implementation of a monitoring and reviewing framework by providing for such work to be carried out by one designated body only. No costs are incurred in putting in place a new system, it is easier for business to work within a familiar system and it will ensure consistency of treatment across financial information. It is also compliant with European legislation. Consequently, this is the approach agreed by the Government in consultation with the FSA and the FRRP.

7.5 The scope of the 2005 Order does not extend to the full range of issuers covered by the Transparency Obligations Directive. It is therefore necessary to make a new order prescribing the FRRP in respect of these other issuers. It would be possible for the FRRP to consider the accounts of these issuers if they were referred to it by the FSA under section 14(7) of the CAICE Act, but it would not be possible for the Panel to undertake proactive reviews of those issuers' accounts under the existing Order.

7.6 The change effected by the new Order is not legally or politically important.

Consultation

7.7 The amendments to FSMA allowing the FSA to make rules to implement the Transparency Obligations Directive and the amendments to section 14 of the CAICE Act were made by the 2006 Act. The provisions were therefore subject to consultation and consideration by Parliament during the passage of the Companies Bill.

7.8 The FSA conducted an open public consultation from 30 March to 30 June 2006 on the rules required to implement various aspects of the Transparency Obligations Directive, including the requirements in relation to periodic financial reporting (FSA consultation paper CP06/4). Overall 60 responses were received from a broad range of stakeholders including accountants, lawyers, issuers and investors. Of those responses, about two thirds made reference to the FSA's proposals regarding financial information and continuing reporting requirements, and were mostly supportive of the general approach to implementing the Directive (the specific question of who should monitor was not covered). The FSA published an account of the representations it received, together with its response to them in October 2006 (FSA paper PS 06/11).

Guidance

7.9 The FSA has issued guidance on how it will implement the provisions of the Transparency Obligations Directive in its newsletter "List!" (Number 14, updated April 2007). It will also be writing to all affected issuers.

7.10 The FRRP does not intend publishing any new guidance, but would refer issuers to the existing material on its website which sets out the Panel's powers and its operating procedures and includes frequently asked questions from companies who receive a letter from the Panel.

8. Impact

8.1 An Impact Assessment has not been prepared for this instrument. The substantive Transparency Obligations Directive requirement to disclose periodic financial information has already been imposed on issuers by FSA rules made under Part 6 of FSMA, and FSMA requires the FSA to maintain arrangements for monitoring compliance with its rules and for enforcing them. An assessment of the effects of the Directive on the costs of and benefits to business generally is included in the Regulatory Impact Assessment for the Companies Act 2006 (available at www.berr.gov.uk/bbf/co-act-2006). It is considered that any additional cost in the FRRP rather than the FSA being designated as the Competent Authority to monitor and review periodic accounts and reports for the purposes of the Directive would be minimal.

8.2 The Order has no impact on the public sector.

9. Contact

Valerie Carpenter at the Department for Business, Enterprise and Regulatory Reform, telephone: 020 7215 0225 or e-mail: Valerie.Carpenter@berr.gsi.gov.uk can answer any queries regarding the instrument.

TRANSPOSITION NOTES***Transparency Obligations Directive (2004/109/EC)***

1. Sections 1265, 1266, 1267, 1268, 1270, 1271, and 1272 in Part 43 (Transparency obligations and related matters) of the Act enable the FSA to implement Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC. Section 1266 inserts seven new sections into Part 6 of the Financial Services and Markets Act 2000; sections 89A, 89B, 89C, 89D, 89E, 89F and 89G. The new sections give power to the competent authority (at present the Financial Services Authority (“FSA”)) to make rules for the purposes of the Transparency Directive (2004/109/EC) (“Transparency Directive”) and connected regulatory purposes. Sections 1267 and 1268 insert three and four sections, respectively, into Part 6 of FSMA (89H to 89N) setting out the regulatory powers of the FSA in connection with the Directive. Section 1270 inserts new sections 90A and 90B into FSMA, which set out the issuers’ liability in damages for disclosures required under the Transparency Directive, and section 1271 inserts a new section 100A into FSMA setting out provisions in relation to the exercise of the FSA’s powers where the UK is a host member state.

2. The Transparency Directive imposes minimum harmonisation requirements on the information to be provided to the public about issuers whose securities are traded on a regulated market and the control of votes attached to shares in those issuers. It permits Home Member States to impose more stringent requirements on entities that they regulate but Host Member States, i.e. those states in which the issuers securities are traded on a regulated market but whose competent authority are not responsible for primary oversight of that issuer, are not permitted to impose any requirements more stringent than those contained in the Transparency Directive.

3. There are three main categories of obligation that are imposed under the Transparency Directive and that the FSA’s transparency rules will implement in respect of UK markets and issuers:

(a) requirements for issuers to make public, at regular intervals, information about their financial position and the progress and management of the business of the issuer;

(b) requirements for holders of votes attached to shares of issuers to notify the issuers when the number of votes they control reaches specified proportions of the total votes available; and

(c) requirements for issuers to treat the holders of the same securities equally.

4. The detailed and technical provisions about the required notifications, disclosures and treatment of security-holders will be prescribed in rules made by the FSA under the new rule-making power at section 89A of the Financial Services and Markets Act 2000. The FSA is required by that Act to carry out consultation and a cost benefit analysis when making any rules under this power.

5. Having the power to make these rules will promote the harmonisation of practice with other EU jurisdictions, and help enhance investor confidence through increased transparency of the financial markets.

6. Responsibility for the transposition of the Transparency Directive lies both with HM Treasury and with the FSA. The measures in the Companies Act that implement the Transparency Directive are the responsibility of HM Treasury.

7. The table below describes the substantive provisions in the Act implementing the Transparency Directive.

Part 43: Transparency obligations and related matters		
Article	Objective	Implementation
1.	Sets out scope of the Directive and two derogations from the requirements of the Directive. The Member States may apply the derogations in respect of securities issued by the government, local government or a state's national central bank.	<i>Part 43</i> of the Act inserts new provisions into the Financial Services and Markets Act 2000 ("FSMA 2000") to give the Financial Services Authority power to make Transparency Rules. Most provisions in the Transparency Directive will be implemented by the FSA's Transparency Rules. Other provisions in the Act or in FSMA 2000 implement the other requirements. If the derogations are to be implemented, the FSA's Transparency Rules will do this.
2.	Provides various definitions used in the Directive.	These will be applied in Transparency Rules, or apply in relation to the implementation of the Article to which they relate.
3.	Limits the circumstances in which Member States may impose more stringent requirements than those contained in the Directive on issuers of securities and holders of interests in those issuers' shares.	Transparency Rules and new FSMA 2000 section 100A(2) introduced by <i>section 1271</i> of the Act.
4.	Requires issuers of securities which are traded on regulated markets to make public its annual financial report consisting of its audited financial statements and the management report.	Transparency Rules: see in particular new sections 89A and 89C of FSMA 2000, inserted by <i>section 1266</i> of the Act.
5.	Requires issuers of shares or debt securities which are traded on a regulated market to make public a half-yearly financial report.	Transparency Rules: see in particular new sections 89A and 89C of FSMA 2000, inserted by <i>section 1266</i> of the Act.
6.	Requires issuers whose shares are traded on a regulated market to make public an interim quarterly statement.	Transparency Rules: see in particular new sections 89A and 89C of FSMA 2000, inserted by <i>section 1266</i> of the Act.
7.	Requires Member States to ensure that responsibility for the information to be drawn up and made public in accordance with Articles 4, 5, 6 and 16 lies at least with the issuer or its administrative, management or supervisory bodies and to ensure that their laws, regulations and administrative provisions on liability apply to the issuers, the bodies referred to in this article or the persons responsible within the issuers.	Provisions relating to liability inserted into FSMA 2000 as new sections 90A and 90B by <i>section 1270</i> of the Act.

8.	Provides various exemptions from the requirements of articles 4, 5 and 6 including to optional exemptions.	Transparency Rules.
9.	Provides that where a shareholder with a significant level of holding acquires or disposes of shares of an issuer whose shares are admitted to trading on a regulated market and to which voting rights are attached, such shareholder notifies the issuer of the proportion of voting rights in the issuer held by the shareholder as a result of the acquisition or disposal where that proportion reaches, exceeds or falls below the thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75%.	Transparency Rules: see in particular new sections 89A and 89B of FSMA 2000, inserted by <i>section 1266</i> of the Act.
10.	The notification requirements in Article 9 shall also apply to a natural person or legal entity to the extent it is entitled to acquire, to dispose of, or to exercise voting rights in any of the cases set out in the Article or a combination of them. (Voting rights acquired through agreement or interest).	Transparency Rules.
11.	Exempts shares provided to or by the members of the ESCB in certain circumstances from the notification requirements imposed by Articles 9 and 10.	Transparency Rules.
12.	Sets out the information that must be included in the notification under Articles 9 and 10 and includes provision on the timing of the notification and when aggregation of holdings required. Paragraph (6) requires the issuer to make public all information contained within a notification within 3 days.	Transparency Rules.
13.	Requires the holders of financial instruments, which are to be specified by the Commission, to notify the issuer of their control of votes in accordance with the requirements in Article 9.	Transparency Rules.
14.	Requires an issuer of shares admitted to trading on a regulated market to make public the proportion of its own shares that it holds when those proportions reach, exceed or fall below the thresholds of 5% or 10%.	Transparency Rules: see in particular new sections 89A and 89C of FSMA 2000, inserted by <i>section 1266</i> of the Act.
15.	Requires the Member State to ensure that an issuer of shares traded on a regulated market, makes public the total number of voting rights and capital at the end of each month during which the number changes.	Transparency Rules.
16.	Requires issuers of securities to make public information about any changes in the rights attached to their securities and any new loan issues and any guarantee or security in respect of such loans.	Transparency Rules: see in particular new sections 89A and 89C of FSMA 2000, inserted by <i>section 1266</i> of the Act.

17.	Requires issuers of shares admitted to trading on a regulated market to treat their shareholders, who are in the same position, equally. It provides for information to be distributed in particular ways and for shareholders to be able to exercise their rights in specified ways.	Transparency Rules. See also <i>Section 1143 and Schedule 5</i> of the Act in relation to communications by an issuer. <i>Paragraph 10 of Schedule 5</i> sets out the requirements for an issuer of shares wishing to communicate by means of a website.
18.	Makes similar provision as that contained in Article 17 but in respect of issuers whose debt securities are admitted to trading on a regulated market.	Transparency Rules. See also <i>Section 1143 and Schedule 5</i> of the Act in relation to communications by an issuer. <i>Paragraph 11 of Schedule 5</i> sets out the requirements for an issuer of debt securities wishing to communicate by means of a website.
19.	Requires issuers to file information that they are required to make public under the Directive, with the FSA and permits the FSA to publish that information itself. It also requires issuers to inform the FSA and the regulated market to which its securities are admitted of any proposed change to its instrument of incorporation.	Transparency Rules.
20.	Sets out the rules for determining which language the issuer must use to disclose regulated information in various circumstances.	Transparency Rules.
21.	Requires issuers to disclose regulated information in a manner ensuring fast access to such information on a non-discriminatory basis. Also requires each Member State to have an officially appointed mechanism for the central storage of regulated information.	Transparency Rules.
22.	Requires the competent authorities of the Member States (for the UK it is the FSA) to draw up guidelines to create an electronic network at national level to share information between the various competent authorities, operators of regulated markets and national company registers. Such guidelines must aim to further facilitate public access to be disclosed under this Directive, Directive 2003/6/EC (the Market Abuse Directive) and Directive 2003/71/EC (Prospectus Directive).	The FSA will draw up guidelines in accordance with the obligations under this Article.
23.	Enables the FSA to exempt issuers based in third countries from certain disclosure requirements if there are equivalent provisions in the third country. Requires the FSA to ensure that where a third country issuer is regulated in the UK for EU purposes, any information which may be important to the public in the Community is disclosed in accordance with Articles 20 and 21.	Transparency Rules.

24.	<p>Requires each Member State to designate a central competent authority responsible for ensuring that the Directive is applied and to give that competent authority specified powers which are necessary for the performance of its functions.</p> <p>Permits each Member State to designate a competent authority for examining that information is drawn up in accordance with the relevant reporting framework.</p>	<p>The central competent authority in the UK will be the FSA, by virtue of the amendments being inserted into Part 6 of FSMA 2000.</p> <p>The FSA already has various powers under FSMA 2000. Other powers for the FSA to perform its functions are contained in new FSMA 2000 sections 89H to 89N inserted by <i>sections 1267 and 1268</i> of the Act.</p> <p>The Act provides power to designate a competent authority for reporting framework purposes by amending the Companies (Audit, Investigations and Community Enterprise) Act 2004. See <i>Schedule 15 (Part 2)</i> of the Act.</p>
25.	<p>Imposes a requirement for professional secrecy on those who work for the competent authority and requires cooperation between the competent authorities of the various Member States.</p>	<p>FSMA 2000 already contains provisions relating to professional secrecy for those who work for the FSA and the Companies (Audit, Investigations and Community Enterprise) Act 2004 also contains provisions in relation to authorities appointed under that Act.</p>
26.	<p>Provides for host Member States to take action in relation to infringements where an issuer or security holder continues to infringe the requirements of the Directive.</p>	<p>New section 100A of FSMA 2000 introduced by <i>section 1271</i> of the Act.</p>
27.	<p>Sets out the committee procedure for the Commission to make implementing measures required by the Directive.</p>	<p>No implementing provision required.</p>
28.	<p>Requires, without prejudice to the right of Member States to impose criminal penalties, Member States to ensure, in conformity with their national law that at least the appropriate administrative measure may be taken or civil and/or administrative penalties imposed in respect of the persons responsible.</p>	<p><i>Schedule 15 (Part 1)</i> of the Act amends section 91 of FSMA 2000 to enable the FSA to impose financial penalties for breach of the Transparency Rules.</p>
29.	<p>Requires a right of appeal to the courts to be in place.</p>	<p>No further implementation is required. FSMA 2000 already makes provision for appeals of FSA decisions to the Financial Services and Markets Tribunal and to the Court of Appeal.</p>
30 – 35	<p>These articles contain transitional and final provisions, including the date by which the Directive must be transposed – 20 January 2007.</p>	<p>No specific implementation is required for most of these provisions. New sections 89B(4) and 89D(1) introduced by section 1266 of the Act make provision for transitional arrangements.</p>