ScottishPower

David T Nish
Finance Director

Your ref

Our ref

Date

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Contact/Extension

Messrs. Paul Ebling, Stephen McEwan, Hans Nailor
Accounting Standards Board
Holborn Hall
100 Gray's Inn Road
LONDON
WC1X 8AL

Dear Sirs

FINANCIAL REPORTING EXPOSURE DRAFTS 23 TO 29

We welcome the opportunity to comment on the above exposure drafts issued by the Accounting Standards Board (ASB).

Our overall comments are set out below. We have also commented specifically on the various exposure drafts but have limited our comments to those areas which believe are the key issues.

In terms of the overall process, we welcome the fact that the ASB has issued the above exposure drafts (FREDs). This has helped to improve the focus on the scale of change that is likely over the next few years as UK GAAP converges with International Accounting Standards (IAS). These FREDs have been developed based on, but not identical to, the recent exposure drafts issued by the International Accounting Standards Board (IASB). While we understand the ASB's reasons for wishing to argue for "better" standards, we strongly believe that it would be inappropriate for the ASB to issue standards which are different from the standards eventually issued by the IASB. The prospect for UK listed companies, of being required to implement new standards under UK GAAP and then having to adopt similar but different standards under IAS one or two years thereafter, is not attractive.

We would welcome the ASB issuing standards on a phased basis but these should not be mandatory until IAS are required to be implemented by UK companies.

We would strongly urge the ASB to lobby the JASB and the EU on behalf of UK listed companies so that the body of accounting standards that are required to be implemented on transition to IAS are published no later than summer 2003. This will enable companies to have sufficient time to implement properly the raft of new standards. The standard setting bodies ought to be fully aware of the time involved in educating and training, changing systems, processes and procedures and communicating with users. We are concerned that the transition to IAS will not be immediately understood by all users and we doubt whether the accounting profession should be self-imposing the risk of further confusion given recent well publicised corporate scandals. We appreciate that the ASB has recognised this with its original transitional approach to implementing FRS 17 ‘Retirement benefits’. This sensible timeline approach should be a feature of the developing financial reporting environment for the benefit of all parties concerned and for financial markets in general.

Our detailed comments on the individual FREDs are included in the attached Appendix.

Should you wish to discuss any of these issues, please contact Stuart MacDonald, Head of Group Financial Reporting, Scottish Power plc, 1 Atlantic Quay, Glasgow G2 8SP (telephone 0141 *566* 4721).

Yours sincerely

DAVID NISH
Finance Director

Appendix

FRED 23 ‘Financial Instruments: Hedge Accounting’

- We do not believe that the ASB should issue a new standard on hedge accounting until the JASB has completed its review of IAS 39.

- In our view, to implement a standard on hedge accounting, a UK standard on the treatment of financial instruments more generally would be necessary. We recognise that the ASB has issued FRED 30 and we will comment on that FRED in due course.

- In our view, there should also be a requirement for the consistent application of methodologies for testing hedge effectiveness both over lime and across similar hedge relationships.

- We believe the ASB should publish a standard which contain rules on how hedge accounting should be performed, not merely setting out the conditions which need to be complied with in order that some (undefined) basis of hedge accounting should be applied.

- We agree with the principle that gains and losses should not be recycled. We request that the ASB argues strongly for this point in the international debate.

- We would encourage the ASB to consider the significant implementation issues that have arisen in the US with respect to SFAS 133 ‘Accounting for Derivative Instruments and Hedging Activities’. In particular, the fact that over 150 DIG interpretations have been issued to provide guidance on applying the requirements of the standard.

FRED 24 ‘The Effects of Changes in Foreign Exchange Rates; Financial Reporting in Hyperinflationary Economies’

- As discussed above, we strongly agree that gains and losses should not be recycled.

- We agree that all entities should translate their financial statements into the presentation currency (or currencies) using the same method as is required for translating a foreign operation for inclusion in the reporting entity’s financial statements.

- We agree with the proposal that the current allowed treatment of translating profits at closing rate should be removed.

- We agree that goodwill and fair value adjustments to assets and liabilities that arise on the acquisition of a foreign operation should be required to be treated as assets and liabilities of the foreign operation and translated at the closing rate.

FRED 25 ‘Related Party Disclosures’

- We believe that an accounting standard should require disclosure of the name of a controlling party and, if different, that of the ultimate controlling party. However, if the eventual IAS does not include such a requirement, then the ASB should not require this disclosure on the grounds of international harmonisation. Please refer to the comments made in our covering letter.

- It is our view that an accounting standard should require disclosure of the names of the transacting related parties where this is material to the user of the accounts. So for example, it would be appropriate to group, for disclosure purposes, all trading transactions with associates. However, if the related parties were, say, directors, then the disclosure of the individual directors’ names would be, in our view, material to the reader of the accounts.

- We believe that any exemptions for subsidiary companies should be only for transactions with fellow group companies, not an exemption from all related party disclosures.

- It is our opinion that the ASB should lobby the IASB to ensure that its eventual standard does not contain an exemption for disclosure of management’s remuneration. This is perhaps the most common related party disclosure of relevance to shareholders. The fact that many countries impose detailed disclosure requirements in this area is no reason for this exemption in accounting standards.

- We believe that the current FRS S application of the materiality concept to transactions with individuals, while logical, is not really practical and should be excluded from any future standards on this topic.

FRED 26 ‘Earnings per Share’

- We see no reason why additional earnings per share figures should be prohibited from the face of the profit and loss account, and would be happy for such additional figures to be disclosed on the face of the profit and loss account provided that they are not given more prominence than the earnings per share figures required by the standard and an explanation of these additional figures is given in the notes to the accounts.

- For companies which prepare interim accounts, we believe that their annual earnings per share figures should be based on cumulative year to date information, not on the basis of previously published interim figures.

FRED 27 ‘Events after the Balance Sheet Date’

- We agree that it would be preferable for the Companies Act to be amended to cater for the intended change in treatment of proposed dividends.

FRED 28 ‘Inventories; Construction and Service Contracts’

- We encourage the ASB to lobby the JASB to encourage the removal of the option to value inventories on a LIFO basis.

FRED 29 ‘Property, Plant and Equipment; Borrowing Costs’

- We believe that residual values should only be based on current estimates where the assets are revalued annually.

- We agree that the proposed standard may prevent entities from using renewals accounting and suggest that it be made clear in the standard that renewals accounting is still permitted. Also, further guidance should be provided as to when infrastructure accounting should be applied and how it would operate. We would recommend the inclusion of the current text in FRS 15 ‘Tangible fixed assets’ on this particular area.

- We believe strongly that the existing use methodology for valuing assets in the UK be applied and would encourage the ASB to lobby for this in the international debate. While market value (exit values) may be appropriate for valuing financial instruments we do not believe they are best suited to valuing tangible fixed assets.

- We believe that a transitional arrangement should be included in a new UK standard to allow entities that adopted FRS 15’s transitional arrangement to continue to recognise the carrying amounts under that arrangement.

- Capitalisation of borrowing costs should remain optional, subject to disclosure of the policy and the amounts capitalised in each period.

- We do not agree that paragraph 5(e) of IAS 23, which allows certain exchange differences to be capitalised, should be deleted in the draft standard on borrowing costs.