IFRS FOUNDATION COMMENTS ON THE MAYSTADT REPORT

The IFRS Foundation notes the report by Philippe Maystadt, Special Adviser to Commissioner Barnier, on his mission to reinforce the European Union's contribution to international accounting standards. We understand that, at the European Council of Finance Ministers (ECOFIN) meeting held on 15 November 2013, Member States gave the European Commission a mandate to pursue the recommendations set out in Mr Maystadt's report. The European Commission is now discussing how to implement the recommendations in the report. Because of these developments, the IFRS Foundation believes it is important to comment on a number of the main recommendations in the report, as well as commenting on a number of references in the report that, in our view, should have been clarified or corrected.

The proposal to "Transform the European Financial Reporting Advisory Group (EFRAG)"

The IFRS Foundation fully acknowledges and respects the fact that it is for the European authorities to determine how the EU's contribution is organised and operated. That said, we do have concerns that the selected option of "Transforming EFRAG" might result in the further lengthening of what are already very lengthy procedures. There is a reference in the report (Maystadt Report, page 20, Recommendation 11) to EFRAG requesting the IASB to have longer comment periods on consultative documents. However, the IASB already has an extensive due process, which was revised earlier this year following a consultation with all global constituents. The IASB is acutely conscious of the fact that it takes years to develop a new IFRS and is looking to reduce the time taken, rather than providing further extensions and thereby slowing down the process even more. Other constituents around the world can meet the IASB's comment deadlines and would not wish to see them being extended to meet a request from Europe. It would considerably hinder the IASB's ability to operate efficiently if it agreed to an EFRAG request for even longer comment periods.

We have urged ECOFIN and the Commission to ensure that the proposals are implemented in a way that will enable Europe to participate in an effective and timely fashion throughout the standard-setting process as well as in the endorsement of IFRSs.

More 'flexible' endorsement

The IFRS Foundation welcomes the fact that Mr Maystadt's report emphasises the support for the maintenance of a "standard-by-standard" adoption procedure. Our research on the jurisdictional adoption of International Financial Reporting Standards (IFRSs) shows that IFRSs are being used in most jurisdictions without modifications. In our view, this provides an important contribution to growth and transparency in the global economy. Most businesses in Europe want IFRSs to remain as global standards. We would therefore warn against having a more flexible endorsement mechanism and urge those responsible for implementing the recommendations to pay heed to the very real risks of flexible endorsement that Mr Maystadt outlines in his report, in particular the negative signal that it would give to the rest of the world (Maystadt Report, page 8).

New criteria for endorsement: transparency must remain paramount

Recommendation 2 in Mr Maystadt's report refers to the possibility of introducing new criteria for the adoption of IFRSs in the EU, ie that they should not endanger financial stability and must not hinder the economic development of the region. In our view, accounting standards should not be "instrumentalised" with a view to hiding or twisting the objective representation of the situation and the performance of businesses. The IFRS Foundation supports the goals of financial stability and economic growth and we believe that IFRSs make a contribution to both by providing transparency to the capital markets. Nevertheless, we remain concerned that there continues to be a misunderstanding as to the purpose of general financial reporting, and about its limitations, and how it interacts with financial stability.

On this issue, we would refer to the 2009 *Report of the Financial Crisis Advisory Group*[1]. The FCAG report sets out very clearly the real situation and how both accounting standard-setters and prudential regulators serve the public interest in accordance with their respective missions. The FCAG emphasised that financial reporting, by providing only a snapshot in time of the economic situation and performance, cannot provide perfect insight into the effects of macroeconomic developments. However, what it does do is provide as unbiased and relevant information as possible about the economic performance and condition of businesses in a way that provides confidence to investors and other capital market participants in the transparency and integrity of that information.

As the Trustees made clear in their *Report of the Trustees' Strategy Review 2011,* that transparency cannot be compromised. In summary, transparency in financial reporting is the IASB's contribution to stability and growth and any proposed new criteria should reflect that. The IFRS Foundation fully understands that extreme volatility can hinder financial stability, but we deeply believe that dealing with volatility and market efficiency is an issue for policy-makers, prudential and market regulators and managers of companies.

Sovereignty has not been renounced

The IFRS Foundation does not take the view that the EU's regulatory sovereignty in accounting was "renounced" (Maystadt report, page 4, 2nd paragraph), because of the endorsement mechanism that is in place. The Commission's 2000 document "EU Financial Reporting Strategy: the way forward" made it very clear that: "The European Union cannot delegate responsibility for setting financial reporting requirements for listed EU companies to a non-governmental third party…To achieve legal certainty for users of IAS in the European Union, international standards must be integrated into the financial reporting legislative framework".

US influence overstated

The reference to the IASB continuing to acknowledge the major influence of North American positions does not strike us as an accurate characterisation (Maystadt report, page 5, 1st paragraph). It is the case that convergence between IFRSs and US GAAP was a strategic goal from 2002, with the signing of the Norwalk Agreement. It is also the case that the IASB and the US FASB have been continuing to work on convergence projects under the 2006 Memorandum of Understanding (MoU), thus fulfilling the objective repeatedly set up by the G20. During that time, the convergence projects have achieved much, but the IASB has maintained its independent voice, even when working with the FASB, on issues on which it has taken a different view that was based on the merits of the issue at

[1] The FCAG Report can be accessed at: http://www.ifrs.org/News/Press-Releases/Documents/FCAGReportJuly2009.pdf.

stake. This is demonstrated by the fact that there remain differences between IFRSs and US GAAP, for example in the treatments relating to the offsetting of financial instruments and the definition of control that is the basis for consolidation.

Nevertheless, while convergence has had positive effects, the worldwide spread of IFRSs made it more appropriate for the IASB to adopt a new strategy and to move to a multilateral engagement with National Standard-Setters (NSS) and regional bodies. The wording in the Maystadt Report does not acknowledge this fact. The shift to a multilateral approach is most notably demonstrated by the establishment of the Accounting Standards Advisory Forum (ASAF), on which 3 of the 12 members come from the EU (plus one 'at large' member , the UK), and 3 from the Americas (representing the US, Canada and the Group of Latin American Standard-Setters, GLASS).

Agenda priorities based on consultation

The IFRS Foundation would also take issue with the comment in the report that the IASB "has a tendency to favour actions that promote international convergence and the search for new members, to the detriment of those actions requested by the states that already apply IFRS" (Maystadt report, page 5, final paragraph, and page 6). On the question of "actions" by the IASB referred to in this sentence, it is the case that, in determining its future work programme, the Board went through a major Agenda Consultation in 2011 and 2012, and selected projects on the basis of the views received and the priorities considered. Over 100 of the 243 responses came from Europe. As an example, many European respondents emphasised the importance of the Conceptual Framework project—which is an IASB priority, and has been put out for consultation until 14 January 2014 in a Discussion Paper.

As set out in the IFRS Foundation's *Due Process Handbook*, the IASB is required to undertake a public consultation on its work programme every three years, which provides an opportunity for all constituents, including those in jurisdictions that already apply IFRSs, to provide their input on the strategic direction and balance of the IASB's work programme.

The fair value accounting debate

The report states that "the financial crisis brought about a debate on what numerous experts considered an excessive resorting to market value for the accounting of financial instruments" (Maystadt report, page 4, final paragraph). It goes on to state that "Some believe that such accounting played a role in worsening the crisis", but does not refer to the opposite view, as shown in most of the academic evidence available[2], that the claim that fair value accounting exacerbated the financial crisis appears to be largely unfounded. Without such a reference, there is a risk that the debate will be perceived as being weighted in one direction, which was not the case.

It should also be remembered that most items on the balance sheet of companies are valued at cost, and that fair value is mainly an issue for financial intermediaries dealing with financial instruments. Even for that case, the IASB has reaffirmed its commitment to a "mixed attribute model" where cost-based measurement is the most prevalent for basic banking businesses. The IFRS Foundation wishes to put an end to the legend of IFRS being exclusively "fair value based", as is wrongly repeated by some IFRS opponents.

[2] See, for example, Laux and Leuz (2010) 'Did Fair-Value Accounting Contribute to the Financial Crisis?' (Journal of Economic Perspectives, Volume 24, Number 1, Winter 2010, pages 93-118) http://nd.edu/~carecob/April2011Conference/LeuzPaper.pdf .