



Australian Government

Australian Accounting
Standards Board

1 March 2011

The Trustees
IFRS Foundation
30 Cannon Street London
EC4M 6XH | UK

AASB 16-17 March 2011
Agenda paper 11.4

Level 7, 600 Bourke Street
MELBOURNE VIC 3000
Postal Address
PO Box 204
Collins Street West VIC 8007
Telephone: (03) 9617 7600
Facsimile: (03)9617 7608

Dear Trustees

Strategy Review

The Australian Accounting Standards Board welcomes the opportunity to respond to the request of the Trustees for comments on its Paper for Public Consultation *Status of Trustees' Strategy Review* (5 November 2010).

The AASB considers that the first ten years of operation of the IASB has been fruitful and the IASB and Trustees can be justifiably pleased with the progress that has been made. Nevertheless, we believe that this is an opportune time to review the strategies of the IASB and Trustees to address the emerging challenges.

The AASB considers that many of the greatest challenges facing financial reporting are in the public sector and that the IASB's horizons should be broadened to aim for improved financial reporting for all types of publicly accountable entities.

The IASB is also faced with the need to have a strategy for managing the trade off between those of its constituents who seek a period of calm in financial reporting requirements and those who seek further change and improvement. The AASB considers that an important part of that strategy should be to recognise that the IFRSs need to be relevant and usable in a wide range of jurisdictions and that such IFRSs need to be developed in a stable environment without stresses created by external pressures to accommodate particular jurisdictions. The AASB considers that in such a stable environment the IASB will be able to better focus on making consistent and high quality decisions and help ensure that IFRSs are adopted in many jurisdictions that may currently be cautious because of the pace of change.

The attachment to this letter presents the AASB's comments on the specific questions in the Paper.

We have participated in the preparation of the Asian-Oceanian Standard-Setters Group (AOSSG) submission. The views in this submission are largely consistent with those of the AOSSG, but differ in some respects, especially in relation to question 1. The AASB is one of few standard setters in the region whose purview embraces public sector and private sector not-for-profit reporting.

Please contact me if you require further information about this submission.

Yours sincerely

Kevin M Stevenson
Chairman and CEO



Issues paper – Status of Trustees’ Strategy Review

Q1 – defining the public interest

- 1.1 The AASB considers the mission in the Constitution is well stated. The AASB also considers that a focus on users in capital markets making economic decisions is generally appropriate, because the focus of attention should be general purpose financial statements, and not special purpose financial statements that users such as regulators can demand to suit their needs.
- 1.2 However, the AASB understands that the reference to ‘world’s capital markets’ in the mission in the Constitution is read by the Trustees and the IASB as relating only to private sector capital markets. The AASB considers this view to be too narrow.
- 1.3 The AASB considers that, at a minimum, ‘world’s capital markets’ should be read as meaning all capital markets where market participants rely on GPFSs, which would include markets for government debt. This is because it is evident from recent events that a lack of relevant publicly available financial information about governments has the potential to significantly impact on the fortunes of market participants. The IASB has tended to focus on the message that international standards are needed because the world’s private capital markets are intertwined, and not to have focused on the fact that capital markets are more generally intertwined.
- 1.4 The AASB believes the Constitution should allow for the extension of the IASB’s role to not-for-profit entities more generally, due to the synergies that would be involved.
- 1.5 The AASB is aware that few standard setters have a responsibility for dealing both with the for-profit and not-for-profit public sectors, and the AASB arguing for an expansion of the role of the IASB into the not-for-profit and public sectors could be regarded as self serving. However, the AASB would argue that, based on its experience with its dual role, it has found there are few areas in which the accounting in each sector needs to be different, and there would be substantial synergies in having the IASB dealing with (accrual¹) financial reporting for all types of reporting entities. Given that the FASB has a responsibility for not-for-profit reporting in the private sector, as do the standard setters of jurisdictions such as the UK, Canada, Australia and New Zealand,

¹ The IPSASB currently deals with both accrual accounting standards and cash-based standards



we see no reason for the IASB not to address that sector. Once that sector is in focus, we would argue that it will become evident that the public sector is little different. The AASB is also aware that any move to extend the role of the IASB would need to involve consultation with the IPSASB and may take time to achieve.

- 1.6 The AASB is of the view that there needs to be a greater recognition that the pace of change must be set at a level that it matches the capacity for that change in the context of all those jurisdictions that have adopted and are planning to adopt IFRSs. This view is not intended as an argument for weaker or compromised standards. Rather the view is based on the idea that constituents around the globe should be able to embrace the standards established by the IASB. The current focus on achieving convergence with US GAAP and the political pressures from some other constituents seems to have led to an environment in which decisions are rushed and the quality of IFRSs is threatened. The AASB is concerned that an outcome of this environment is that many prospective IFRS adopters will significantly delay their commitments to IFRSs.
- 1.7 In addition, while we agree that the primary purpose of financial reporting should be the effective functioning of world capital markets; we think that financial reporting also has broader impacts, either directly or indirectly. These include regulatory impacts (such as where legislation applicable to corporate entities links the calculation of distributable appropriations to entities' accounting profits), tax code impacts (such as where the calculation of taxable income is linked to entities' accounting profits), management reporting impacts (for financial planning purposes), impacts on debt and other covenants. Accordingly, in order to promote the global acceptance of the standards, we believe the mission should explicitly acknowledge these aspects.

Q2 – financial stability

- 2.1 Governments, through their banking and prudential regulators, generally have a primary role in helping to ensure financial stability. The AASB considers it would be inappropriate to make financial stability and similar public policy concerns an objective of accounting standard setting. Financial stability could be noted as being a consideration for the IASB, but only in the context of meeting the IASB's primary



objective, and only provided it does not conflict with the IASB's Conceptual Framework.

- 2.2 The AASB views financial stability to be something that high-quality financial reporting would be expected to help achieve, but not a basis for selecting accounting policies. A concern about the notion of financial stability as an objective to be used to determine particular accounting policies under IFRSs is that it seems to be interpreted by many as being a basis for avoiding transparency, particularly as it relates to income statement volatility. This includes recent arguments about having the IASB develop standards that avoid 'pro-cyclicality'.
- 2.3 The Board considers the Trustees have a role in:
- (a) ensuring that exponents of financial stability know that transparency in financial reporting is important in helping to achieve financial stability; and
 - (b) dispelling the idea that financial stability is threatened by accounting policies that reveal volatility.
- 2.4 A focus on financial stability may harm financial reporting because it may lead to Standards that result in inadequate information being made available to users, and bias their decision making.
- 2.5 If there is a concern that users or preparers might behave illogically as a result of reporting more relevant information, the answers should be sought in better education and better communication when reporting. Trying to avoid transparency for the sake of financial stability cannot be conducive to meaningful reporting.

*In responding to Q3 and Q4, the AASB considers that independence and accountability are **not** competing concepts. Accountability can be achieved without losing independence – provided the technical decision-making is insulated from political interference (see comments on Q5).*

Q3 – governance of the IFRS Foundation

- 3.1 The AASB considers the current governance structure, which consists of the Monitoring Board, IFRS Foundation Trustees, and the IASB remains appropriate. However, the AASB thinks that the role of the Monitoring Board is not clear.



3.2 The AASB believes the function of the Monitoring Board should be to provide independent assurance that the Trustees and the IASB are discharging their functions effectively. The Monitoring Board should have no executive function and its membership should comprise those with sufficient knowledge of IFRSs and the role of IFRSs for them to be respected for their views. Accordingly, we would expect that the Monitoring Board would be largely, but not exclusively, comprised of people from countries applying IFRS. It should not be a larger group.

Q4 – formal political endorsement

4.1 The AASB considers that truly global financial reporting will be achieved with one set of high-quality standards and uniform regulation and enforcement that help ensure uniform compliance with standards rather than just the development of uniform accounting standards. Since the regulation and enforcement of financial reporting is normally a government activity (through government agencies), the formal endorsement of governments is likely to be needed. The AASB would hope that such endorsement would be able to be obtained with a view to advancing the common good and therefore be ‘unpoliticised’.

4.2 Uniform regulation would appear to be a longer term goal and we believe that the current focus should be the development of high quality globally accepted accounting standards. In that way, the IASB and Trustees can show leadership and government endorsement would be more readily obtainable than would otherwise be the case.

Q5 – structure of standard setting process

5.1 The AASB considers that the separation achieved between the oversight/funding of standard setting (through the Trustees) and the technical aspects of standard setting (through the IASB) is critical and must be maintained because they are fundamentally different roles and the separation is needed to avoid many of the conflicts that might otherwise arise.

5.2 The AASB questions whether further scrutiny of the structure of the standard setting process is particularly critical at this stage. A well-tested structure for due process has been in place for nearly 10 years. The AASB suggests that, although improvements to



process are always welcome, the main cause of discontent with the IASB's outputs, is not flaws in the form and structure of the due process.

- 5.3 The AASB considers there is currently undue haste for reform and an inappropriate preoccupation with convergence with US GAAP. The AASB also considers there has been too much emphasis on 2011 being a 'watershed' for IFRSs.
- 5.4 The AASB believes the Trustees and the IASB should focus on creating an environment in which the IASB can identify and progress high-quality answers at earlier stages of the standard-setting process. The steps that need to be taken to help create this environment include developing techniques for assessing the impacts of proposed new accounting standards and broadening the IASB's focus to facilitate the efforts of transitioning jurisdictions.

Q6 – application and implementation issues

- 6.1 The number and extent of application and implementation issues seems likely to increase as more jurisdictions apply IFRSs, particularly those with a long history of more rule-based standards. Most jurisdictions (including Australia) at the time of adopting IFRSs have in place 'background' literature and practice that is both formal and informal in nature. This provides practitioners with reference points for resolving application issues. Once a jurisdiction transitions to IFRSs, in order to ensure IFRS compliance, it would generally need to abandon that background material and there is an incentive to seek to replace it as quickly as possible with interpretations or implementation guidance, which the IASB would generally be asked to provide.
- 6.2 Jurisdictions with a history in IFRSs no longer seek many interpretations and the national standards setters and the IFRS interpretations committee have reasonably effective protocols in place to maintain this position. The AASB considers that it is important for the IASB to proceed in a manner that helps to maintain these protocols and encourage transitioning jurisdictions to benefit from the experience of jurisdictions with an IFRS history. The danger is that, as many important standards are being revised, those protocols will be lost and there will be calls for more interpretations and principle-based standard setting will be undermined or there will effectively be many sets of



IFRSs; thereby frustrating the original aim of a single set of global financial reporting standards.

- 6.3 The AASB is firmly of the view that the answer to problems of transitioning jurisdictions does not lie in more formalised interpretations of IFRS. The AASB considers that it is essentially an educational challenge in which strategies are needed to make IFRS training and ‘informal IFRS’ accessible. The AASB considers there may be merit in seeking to make the technical databases and experiences of the larger accounting firms and other large educators into sources for the training of accountants and regulators around the world.
- 6.4 The AASB considers the emphasis should be on the IASB creating an environment in which application and implementation issues are, to the extent feasible, dealt with before finalising new and revised IFRSs, rather than on subsequent interpretations. For this to occur, the IASB needs to provide longer comment periods for proposals (as already allowed for in respect of major projects in the IASB’s *Due Process Handbook*) to help ensure that proposals are thoroughly debated and tested. Also see the comments below at Q8.

Q7 – automaticity of financing

- 7.1 The AASB supports the Trustees efforts to establish a better funding model for the IASB. The AASB considers that the funding model should be reflective of the parties for whom standards are being set.
- 7.2 The AASB considers that each jurisdiction applying IFRSs should be funding a share of the costs of establishing and maintaining IFRSs. The basis for that sharing should be a proxy for capacity to pay, such as relative GDP. It may well be that an additional social overlay might be needed to assist developing countries to make the transition. This might be needed, for example, where the domestic accounting profession or government is particularly poorly placed to bear its share of costs on a relative GDP basis.
- 7.3 The AASB believes that the Trustees should be actively seeking proportionate funding from the 120 or so jurisdictions applying or committing to apply IFRSs. If that could be achieved it would probably mean the budget would not be a significant issue and that the burden would be equitably spread.



Q8 – other issues – consultation periods

- 8.1 In making comments to the IASB, the AASB's capacity is often stretched in undertaking the processes necessary to understand the full implications of IASB proposals and undertaking the relevant consultation with its own constituents on IASB proposals within the set comment timelines. Furthermore, the AASB is probably one of the best-equipped jurisdictions to make comment to the IASB, in terms of Board and staff resources and constituent interest and experience and due to the fact that we do not face translation issues.
- 8.2 Since being involved in the process of leading and participating in AOSSG Working Groups tasked with responding to IASB EDs, the timing issues have been magnified for the AASB. Furthermore, we have gained a greater appreciation of the issues faced by jurisdictions with fewer resources, particularly those who typically work in languages other than English.
- 8.3 The IASB's reasons for setting its comment timelines can be complex, but a driving factor often mentioned is the need to achieve IASB-FASB convergence on key topics by June 2011. The AASB considers that this convergence objective should be a second order issue for the IASB, and that it should not adversely impact on the need for adequate consultation.
- 8.4 The IASB needs to be more conscious of its role as a global standard setter that has a wide set of constituencies that are at varying stages of development and vary in their use of IFRSs. The IASB is not the same as a national standard setter that may be able to take a relatively narrow perspective because it is dealing with a particular domestic constituency.
- 8.5 The AASB considers that the Trustees' focus should be on jurisdictions transitioning into IFRSs rather than on convergence with particular jurisdictions on the basis that efforts directed at facilitating transition to IFRSs will have a greater payback in meeting the goal of a single set of global accounting standards.
- 8.6 The AASB considers that the recent comment periods for IASB EDs have been inadequate, particularly on major topics such as leases, revenue and insurance contracts.



Q8 – other issues – regional bodies

- 8.7 The AASB notes that the Asian-Oceanian Standard-Setters Group has established itself with a view to contributing to the IASB's efforts in establishing a single set of global accounting standards, and the Trustees could consider how that model might usefully be extended to cover the world. It seems likely that the IASB will need to work primarily through regional arrangements for reasons of practicality.
- 8.8 Regional bodies could assist the IASB in advising of the various due process requirements that must be undertaken before new IFRS standards can be adopted in each jurisdiction.
- 8.9 Regional bodies could also assist the IASB more with its outreach activities, which are welcome, but can cause difficulties in the context of planning domestic due process. For example, an outreach by IASB Board and staff members may well make it impractical to run domestic roundtables even though the IASB outreach may not have taken the form of a roundtable. It may be better for those outreach sessions to be regionally focussed, leaving the domestic standard-setters to meet their responsibilities within their individual jurisdictions.
- 8.10 Based on the above, the AASB considers the Trustees and IASB should contemplate establishing protocols that are more directly attuned to any existing regional standard-setting groups. Those protocols could cover the means by which coordination can be achieved in due process and outreach, promotion of domestic standard-setting, handling of requests for interpretation, post-implementation and other research, and in identifying talent within the region relevant to needs of the Trustees and Board. The AASB believes the Trustees need to focus on considering ways in which they could be nurturing standard setting talent in the interests of creating a pool of people who will help to maintain the technical credibility of the IASB.

Q8 – other issues – conceptual frameworks

- 8.11 The IASB is working with the FASB to develop a common conceptual framework, and this is laudable. However, although still in development, it is evident that the revised framework is likely to have a greater focus on private for-profit sector entities than the existing IASB framework. In many ways it seems to have unnecessarily taken a less



generic line than the existing IASB framework. At the same time, the IPSASB is developing its conceptual framework with a focus on the public sector. In the AASB's experience, if the frameworks need to be different, this would only be at the margins.

- 8.12 The AASB considers that two separate frameworks are being developed unnecessarily, and if this is allowed to continue, it will create a convergence problem that may take years to repair. Essentially, a problem is developing that could be prevented if leadership were shown and action taken now to develop one framework that covers all reporting entities.