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Sven Giegold
Member of the European Parliament
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Dear Mr Giegold,

First of all, please accept my appreciation for your interest in the work of the IFRS Foundation and the International Accounting Standards Board (IASB). The European Parliament is an important stakeholder in our work to develop a global language for financial reporting, and I am happy to answer the questions that you have raised.

While writing, I would like to invite you and your colleagues to come and visit our offices in London. We were fortunate to host a visit from Commissioner Barnier a few months ago. I believe the visit was beneficial to the Commissioner, to understand better what we do and why we do it. I would be happy to arrange a comprehensive programme for you, if you were able to join us.

In the meantime, please find below our responses to your questions. If I have misunderstood your question provided in German, please let me know.

Q: The award winning report "Unburnable Carbon" has pointed to the questionable valuation problems of carbon related assets in balance sheets. How will the IASB take the respective valuation risks into account?

Globally, many governments have developed schemes to encourage a reduction in the production of greenhouse gases. Some of these schemes have financial reporting consequences, including how to account for allowances awarded by a scheme administrator and when and how to account for liabilities associated with the related emission of greenhouse gases.

The IASB is developing a Discussion Paper that will provide an inventory of trading schemes, an analysis of the common economic characteristics of the schemes and an initial assessment of the potential financial reporting solutions.

We have already undertaken a significant amount of preparatory work documenting the characteristics of different schemes and assessing their economic implications.

However, there are many different types of schemes internationally and it is important that we develop financial reporting that allows for global comparability. We expect the Discussion Paper to be published in 2014.

Furthermore, the IASB is closely involved in the International Integrated Reporting Council (IIRC), participating in meetings of the Council and various working groups.

Q: How do you see the future role of the Monitoring Board? Is there need for change?

The Monitoring Board is the supervisory body of the IFRS Foundation, of which I am Executive Director. It is therefore difficult for me to comment on a body that supervises us.

However, I am aware of lingering concerns expressed by members of the European Parliament about the governance and supervision of the IFRS Foundation and the IASB. In response to these concerns, the Monitoring Board and the Trustees each conducted separate but co-ordinated reviews of the respective governance and strategy of the IFRS Foundation. Both the Monitoring Board and the Trustees consulted widely over a two year period, and the conclusions of both reports were published in February 2012[1].

My personal observation is that the conclusions of both reports were broadly welcomed, and provide the IFRS Foundation with a governance framework that is appropriate for a global accounting standard-setter—providing the appropriate balance between independence and public accountability. We are in the process of implementing in full the conclusions of both reports that are actionable by the Foundation.

Q: Is a greater involvement of EU institutions in the preparation of the Standards being considered in the future?

As I mentioned before, the European Parliament is an important stakeholder in our work to develop a global language for financial reporting. As such, European interests are already well represented at all levels of the organisation.

The European Commission is represented on the Monitoring Board by Commissioner Barnier, while one quarter of IASB and one third of Trustee positions are allocated to Europeans. The IFRS Advisory Council—the formal advisory body to the IASB—includes representatives from the European Accounting Association, the European Central Bank, the European Financial Reporting Advisory Group (EFRAG), the European Insurance and Reinsurance Federation, the European Round Table of Industrialists, and the European Securities and Markets Authority (ESMA). The European Commission also serves as an observer at meetings of the IFRS Advisory Council and the IFRS Interpretations Committee.

The recently completed Trustees' Strategy Review recognised the benefit of further deepening the involvement of jurisdictions throughout the life cycle of the standard-setting process. Accordingly, the IFRS Foundation is in the process of creating an Accounting Standards Advisory Forum (ASAF),

[1] *Monitoring Board and the Trustees of the IFRS Foundation announce conclusions of their Governance and Strategy Reviews*, February 2012, www.ifrs.org

which will comprise of representatives from national standard-setters and regional bodies. The proposals, published for public comment in November 2012, propose that 25% of the seats on the ASAF will be allocated to Europe.

In summary, I think it reasonable to conclude that Europe is well represented at all levels of the organisation.

Q: How are IASB members chosen?

Members of the IASB are chosen through an open and rigorous process that includes advertising vacancies and consulting relevant organisations. The Trustees proactively seek nominations from the region for which they are recruiting an IASB member. In the case of Europe, the Trustees will, as a matter of course, make contact with the main European institutions (such as the European Commission, the European Parliament ECON Committee and the ESMA) and request nominations.

The main qualifications for membership of the IASB are professional competence and practical experience. The Trustees select members of the IASB in a manner that is consistent with the criteria for IASB members set out in the IFRS Foundation *Constitution*, so that it will comprise a group of people representing, within that group, the best available combination of technical expertise and diversity of international business and market experience in order to contribute to the development of high quality and global financial reporting Standards.

Q: What role do relationships to auditing firms, investors and regulators play in the appointment of IASB members?

Personal relationships that candidates have with auditing firms, investors and regulators play no part in the selection of IASB members. Selection is based upon technical expertise and competence, regardless of where this has been built. As a result, the IASB does have an appropriate balance of representation across relevant stakeholders groups.

Q: Why are there no members with practical experience in NGOs or consumer protection bodies?

The Trustees encourage applications from a wide range of interested parties with diverse backgrounds. The selection process does not exclude the inclusion of members with experience of such organisations.

However, a primary concern of the Trustees is to select IASB members with the requisite knowledge of accountancy and accounting standard-setting. Furthermore, when the IASB develops Standards it seeks input from a wide range of sectors. When the IASB is concerned that it does not have sufficient input from a particular sector it will take steps to solicit further views.

However, even with the accent on the requisite knowledge, we do have three members on the Board that have worked in Non-Governmental Organisations or consumer protection bodies.

Q: Why does the IASB—since its reorganisation in 2001—not foresee any representation of trade unions? What activities are under way to rebalance this situation?

As noted above, the main qualifications for membership of the IASB are professional competence and practical experience. While the Trustees seek to select IASB members who provide an appropriate mix of recent practical experience, they are not selected to represent particular sectors or jurisdictions. Instead, they are required to commit themselves to act in the public interest.

Q: What influence does the Monitoring Board have in reality and on the work of the organisation? How are decisions taken? Where and how are their decisions documented and are these publicly available?

The Monitoring Board is a separate entity from the IFRS Foundation, so it is not for me to answer on their behalf. From our perspective, we have a good working relationship with the Secretariat of the Monitoring Board and the interaction functions well. The Monitoring Board approves all Trustee appointments and will often meet candidates before approval. The Trustees meet formally with the Monitoring Board at least once a year, and those meetings are held in public sessions.

The Monitoring Board Governance Review recognised the need for greater transparency in its own activities and I believe that they have already taken steps to put this in place. However, I would refer you to the European Commission as the designated member of the Monitoring Board to understand better where they are in that process.

Q: The IASB pays great attention to the transparency of its process. However, this is only a 'consultative' and not a participatory process. There is little known about how information is internally evaluated and used. Who reviews comments? What happens with dissenting opinions? How is information used and on what basis are they used for decision making by the IASB? To what extent is the IASB using information from the financial industry?

The IASB follows an extensive due process in developing Standards. While the IASB is independent in its decision-making, we see due process as a participatory process in which the IASB seeks and considers a wide range of views from interested parties throughout all stages of the development of a Standard. The input received from interested parties is published on the website, reviewed by staff and considered during meetings of the IASB. Furthermore, a *Feedback Statement* is published at the end of the project that describes how the IASB responded to the broad themes of the feedback received.

All Staff Papers are posted on our website and all discussions of technical matters by the IASB are held in public. Dissenting opinions are given in public and published on the website. This ensures that the decision-making by the IASB is transparent. The IASB uses these procedures to gain a better understanding of different accounting alternatives and the potential effect of the proposals on affected parties. The IASB's due process is overseen by a committee of the Trustees of the IFRS Foundation, the Due Process Oversight Committee (DPOC), which plays a very active role in ensuring that the IASB follows due process procedures that reflect best practice.

In May 2012, the Trustees issued for public comment a draft of a revised *Due Process Handbook* that proposed enhancements to further improve the IASB's due process, which is built on the principles of transparency, full and fair consultation and accountability. The Handbook, which is in the process of being finalised, sets out—among other things—how the IASB seeks and assesses comments and its voting procedures, including dissenting votes, and how it reports transparently on these issues both to the DPOC and more widely. The draft of the revised Due Process Handbook is available from the IFRS website at www.ifrs.org.

Throughout the due process, comments and views are given by a wide range of interested parties, including the financial services industry.

Q: The basis for IFRS evaluations are assumptions about future events. This leads to volatile results and makes it more difficult to compare financial reports. Why is fair value so important and why do we not pay attention to "insecurity about future assumptions"?

Fair value is just one measurement method used in financial reporting. As Hans Hoogervorst recently made clear in a speech,[2] the IASB has always been a proponent of the mixed measurement model. It is by no means perfect, but in many cases it is considered to provide the most useful information to investors. As part of its response to the global financial crisis, in 2011 the IASB issued improvements to fair value measurement in the form a revised Standard IFRS 13 *Fair Value Measurement*.

With regard to insecurity about future assumptions, this is a topic that Hans Hoogervorst, Chairman of the IASB, addressed in a speech entitled 'The imprecise world of accounting'. I attach a copy of that speech for your reference.

Q: Why are we using the fair value principle also for the *IFRS for SMEs*? What are the motives and where are the boundaries for subjecting everything to the needs of the financial markets? Which areas should not be included in the fair value logic? Is the IASB aiming at deciding if and when fair value should be used and where not?

Fair value is just one of several different measurement methods used by IFRS and the *IFRS for SMEs*. In many cases, such as the measurement of derivatives, fair value is the only valid measurement method, for example, where a company has sought to hedge against currency risk or rises in interest

[2] *Dispelling myths about IFRS*: Introductory remarks by Hans Hoogervorst, Chairman of the IASB, www.ifrs.org

rates. The IASB's recent work to reform its Standards for the accounting for financial instruments deals specifically with the question of which measurement methods should be applied to which types of financial instruments.

For the *IFRS for SMEs*, use of fair value measurement is limited to financial instruments—although some other topics do make reference to fair value—such as the fair value model for associates and jointly controlled entities, investment property and the fair value of pension plan assets.

Q: How can the IASB create Standards that allow for truly comparable financial reports over a longer time-frame?

The IASB has a *Conceptual Framework for Financial Reporting* (*Framework*), which is designed to assist in the development of future Standards and the review of existing Standards. There is a project in progress to review and revise the existing *Framework*. The existing *Framework* sets out a number of qualitative characteristics of useful financial information. One of these is comparability. One of the most important reasons that financial reporting Standards are needed is to increase the comparability of financial information.

Furthermore, the IFRS Foundation has taken a number of additional steps to improve the comparability of financial reporting internationally. First, the Trustees recently concluded a review of the IFRS Interpretations Committee (the Interpretations Committee), which will lead to the Interpretations Committee playing a more active role with a wider variety of tools at its disposal. Second, the IASB has formed a Board-level Implementation Committee to examine and recommend steps that the IASB can take to improve the consistency of the implementation of its Standards. Finally, and linked to this work, the IASB is deepening its co-operation with enforcement bodies, such as the European Securities and Markets Association (ESMA) and the International Organization of Securities Commissions (IOSCO).

Q: Isn't there still too much room for judgements in financial regulation and does it not depend too much on subjective assessments of future events? Is comparability of bank's financial reports actually possible?

This topic was addressed in a recent speech[3] by Hans Hoogervorst, where he stated:

> Like other forms of economic science, there is an awful lot of judgement that goes into preparing financial statements. Accounting has the same problems as its sibling Economics: you need maths to exercise it, but you should not count on outcomes with mathematical precision.

[3] Accounting Harmonisation and Global Economic Consequences, Hans Hoogervorst, November 2012, www.ifrs.org

Hans goes on to state that:

> The application of professional judgement is an essential characteristic of financial reporting … That is why we intend to devote a lot of time revising our *Conceptual Framework*. The *Conceptual Framework* is the theoretical foundation of our Standards.

Q: What does the IASB think of the proposal of more transparent disclosure of profit presented at fair value valuation by having a reconciliation between non-realised and realised gains?

IFRS already require the separate disclosure of unrealised fair value gains for valuations that rely more heavily on models. This is a topic that has already been identified for consideration in the IASB's disclosure project, as part of the review of the *Conceptual Framework*.

Q: The Standards are changing often. This makes a lot of frequent organisation changes necessary and is a considerable cost factor for companies. How do you assess cost and benefits and how are these assessments considered in deciding about future projects?

It is only right that accounting Standards evolve over time in line with changes in business practices. As an organisation we are mindful of the costs that businesses incur as a result of these changes to Standards and we make great efforts to only fix what needs fixing.

The IASB has recently added a research phase to its standard-setting due process that will be increasingly undertaken with the help of other standard-setting bodies. This will streamline the standard-setting process, making it easier to identify and rectify problems.

Effects analyses are now a regular part of the IASB's due process. The IASB is committed to assessing and sharing knowledge about the likely costs of implementing proposed new requirements and the likely ongoing, associated costs and benefits of each new Standard—the costs and benefits are collectively referred to as 'effects'. The IASB gains insight on the likely effects of the proposals for new or revised Standards through its formal exposure of proposals and through its fieldwork, analysis and consultations with relevant parties through outreach activities. The likely effects are assessed:

(a) in the light of the IASB's objective of financial reporting transparency; and

(b) in comparison to the existing financial reporting requirements.

Work in this area is still developing. The IASB has set up a consultative group to advise it in developing an agreed methodology for effect analysis and field testing.

Q: What is the relationship between changes in Standards and *IFRS for SMEs*?

There is no direct relationship in making changes in Standards and the *IFRS for SMEs*. Although based upon the same principles, they are separate Standards. Changes implemented to Standards do not automatically carry over to *IFRS for SMEs*. The IASB is currently undertaking a comprehensive review of the *IFRS for SMEs* and has issued a Request for Information (RFI) to gain public views on whether there is a need to make any amendments to it and, if so, what amendments should be made. The RFI can be accessed from our website and the deadline for responses is 30 November 2012.

Q: Are you still aiming for global Standards or has this become an unrealisable objective after the US decision?

Establishing global accounting Standards is still very much at the forefront of the IFRS Foundation's aims. That remains the primary objective of the IASB. In their *Strategy Review* report, the Trustees of the IFRS Foundation reaffirmed the organisation's commitment to the long-term goal of the global adoption of Standards.

However, the US is no longer critical to the success of the organisation. As Hans Hoogervorst said in a speech in December 2012[4]:

> Five years ago, a standstill in the United States would have had very serious consequences for the IASB. The risk was that without the US on board, Europe would go its own way and Asia would develop its own regional Standards. Today, such talk has gone. For the many countries I referred to, the cost of transition to IFRS is behind them.
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> There is no appetite to undo this work and revert to national or regional Standards. IFRS already has a global impact and that will not change. So there is no longer any risk of IFRS disintegrating as a result of a standstill in the United States.
>
> Nevertheless, there is much concern about strong and continued US leadership in our work and processes if the US is not going to come on board in some shape or form.
>
> I believe the United States should remain an important participant in our institutions and activities. But obviously, US influence will be commensurate with its commitment to our Standards. To give just one example: it will make a huge difference whether the FASB will be in a position to endorse our Standards, instead of being a national standard-setter without a role towards IFRS.

The US SEC staff report published in July 2012 can be considered a 'no decision' rather than a 'no' decision. Indeed the analysis of the report conducted by the IFRS Foundation staff and published in October shows that there are no insurmountable obstacles for the adoption of IFRS by the US, and that the US is well placed to achieve a successful transition to it, thus completing the objective

[4] Opening remarks at the AICPA/SEC conference, Hans Hoogervorst, December 2012, www.ifrs.org

repeatedly confirmed by the G20 leaders. The full analysis of the SEC report conducted by IASB staff can be found on our website at www.ifrs.org.

I trust that we have provided satisfactory responses to your questions and I look forward to meeting with you once again in the near future.

Yours sincerely,

Yael Almog
Executive Director
IFRS Foundation

Enclosed:

- Speech by Hans Hoogervorst, 'The concept of prudence: dead or alive?', September 2012, see http://www.ifrs.org/Alerts/PressRelease/Pages/prudence-speech-Sept-2012.aspx
- Speech by Hans Hoogervorst, 'The imprecise world of accounting', June 2012, see http://www.ifrs.org/Alerts/Conference/Pages/HH-speech-Amsterdam-June-2012.aspx
- Proposed revisions to Due Process Handbook, see http://www.ifrs.org/DPOC/DueProcessHandbook/Documents/DueProcess.pdf
- Speech by Hans Hoogervorst, 'Accounting harmonisation and global economic consequences', November 2012, see http://www.ifrs.org/Alerts/Conference/Documents/HH-LSE-November-2012.pdf