acteo Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

Mouvement des Entreprises de France
MEDEF

IFRS Foundation
30 Cannon Street
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Paris, February 11, 2011

Re: **Trustees Strategy Review**

Please find attached, the answer MEDEF/ACTEO relative to the public consultation "Trustees Strategy Review".

Should you wish any supplementary comment or explanation, please do not hesitate to contact us.

ACTEO
Patrice MARTEAU
Chairman

MEDEF
Agnès LEPINAY
Director of economic and financial affairs

TRUSTEES STRATEGY REVIEW

<u>**Mission: How should the organisation best define the public interest to which it is committed?**</u>

1. ***The current Constitution states: "These standards [IFRSs] should require high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions." Should this objective be subject to revision?***

   We have the following remarks in response to this question and the reference it makes to the Constitution:

   - As the extract above indicates, the Constitution states that financial statements drawn up in accordance with IFRS should help users to make economic decisions: operational decisions in the case of the management of the reporting entities, and decisions about the provision, maintenance or withdrawal of capital in the case of the investors. It is therefore essential that there be a common language between those who take operational decisions and those who analyse the value that these decisions engender, between those who account for their stewardship and those who invest. For this language to be truly common, it is essential that those who govern the entities be considered to be users of the accounting standards on an equal standing with the investors and that their needs be taken into account equally. The IASB must look after the interests of the whole of the user community, in other words, it must consider the interests of all the stakeholders without privileging any particular sub-group arbitrarily.

   - This is not the case today. In common with the section of the conceptual Framework dealing with the objectives of IFRS, the Constitution clearly establishes a hierarchy among the users by setting the providers of capital at the top, The entities are not considered to be users of their own financial statements but as mere "preparers", whereas they have the joint responsibilities of producing the financial information, ensuring its compliance with legal and other requirements, and communicating it to users in the most appropriate way.

   - Reporting entities and their managements are the primary users of accounting information and are the principal correspondents with analysts on a daily basis. They are therefore stakeholders who are particularly concerned and particularly well placed to give an opinion on the quality of accounting standards. The accounting system and the financial information that results from it are key tools of management. The first priority for these tools is to measure the performance of the entity in the way that both the management and the analysts can understand.

Standards which have been dismissed as resulting in a misleading representation of the entity's activities bymost companies and organizations which represents them, such as parts of the financial instruments standards, parts of the business combinations standard, share-based payments and the proposed changes to IAS 37, cannot be deemed to have satisfied the mission of the IASB as it is described above.

- The growing use of non-GAAP measures by entities across all jurisdictions appears to demonstrate that the IFRSs as they stand today do not fulfil the requirement for a common measure of performance. It also indicates that the IASB's mission is not being properly fulfilled since the standards are resulting in a loss of comparability in financial information and, as collateral damage, a risk of the undermining of the internal control culture in entities. From our point of view, therefore, it is time to rank the reporting entity explicitly alongside the investor as users of IFRSs The Constitution and the conceptual Framework, if opposed to this evolution, should then be modified. **.**

2. ***The financial crisis has raised questions among policymakers and other stakeholders regarding the interaction between financial reporting standards and other public policy concerns, particularly financial stability requirements. To what extent can and should the two perspectives be reconciled?***

   - First of all we would point out that this question would not have had to be asked if IFRSs had taken into account the business model of companies. The dysfunctional outcomes that have resulted from the use of the fair value [mark-to-market] measurement are linked to instantaneous and excessive changes in valuation, either upwards or downwards, in unregulated, over-reactive markets which did not reflect the economic fundamentals of a large part of the financial instruments concerned. The first response to this question should be to return to an accounting paradigm which properly reflects the business model.

   - Furthermore, we do believe that accounting standards cannot be used to fulfil too many different objectives and that the main objective has to be to give an appropriate image of the performances and business model of the concerned entities. Nevertheless, during the process of the development of standards it would be appropriate to ask the question of what the impact of the proposals might be on market stability. This should be done in concert with the relevant prudential authorities and regulatory bodies in order to identify and resolve the potential conflicts between relevance and consistency of accounting on the one hand, and market stability on the other. In order to be effective and efficient, this activity should be engaged in at the very outset of the process of developing a standard.

<u>Governance: how should the organisation best balance independence with accountability?</u>

3. ***The current governance of the IFRS Foundation is organised into three major tiers: the Monitoring Board, IFRS Foundation Trustees, and the IASB (and IFRS Foundation Secretariat). Does this three-tier structure remain appropriate?***

4. ***Some stakeholders have raised concerns about the lack of formal political endorsement of the Monitoring Board arrangement and about continued insufficient public accountability associated with a private-sector Trustee body being the primary governance body. Are further steps required to bolster the legitimacy of the governance arrangements (including in the areas of representation of and linkages to public authorities?***

   In our view, the IASB, the IFRS Foundation Trustees and the Monitoring Board have very distinct roles and for this reason the three bodies must be kept in place. However, it is a matter of fundamental importance that the composition of the bodies and their respective missions be revised:

   - **The Monitoring Board** must be the instance of the representation of those who have decided to "buy into" the IFRS accounting model. The composition of this body should reflect the profile of the stakeholders while making room for the representation of the authorities responsible for the financial markets in order to ensure that the necessary dialogue on this subject can take place. In addition to its existing participation in the nomination process for Trustees, the Monitoring Board should also have a right of oversight over:

     - The Constitution;
     - Governance, with notably a right of veto over the selection of the Chairman of the IASB; and
     - The financing of the IFRS Foundation.

   - **IFRS Foundation Trustees** should, for their part, include a much higher proportion of representatives of reporting entities. It is, however, appropriate to maintain representation of the regulators' point of view, as is currently the case. In addition, the role of this body should be significantly strengthened, but without putting at risk the principle of the technical independence of the IASB. Roles which the IFRS Foundation Trustees fulfil should include the following:

     - **Supervision of the IASB's work programme; this should be submitted for public consultation and should be consistent with a general framework of objectives and principles to which all the stakeholders subscribe.** The current agenda, which was set without any consultation of, or consensus from, the whole group of stakeholders, set the objective of convergence as all-important and has resulted in the complete reworking of a number of standards. The necessity of a number of the projects is contested by most of the stakeholders, whilst essential improvements and additions to other standards seem to have been consigned to oblivion.

- **Supervision of the major orientations of the conceptual Framework and of the definition of the major principles behind IFRS**, (such as, what is performance? What is the role of fair value? What is financing?, etc.) The IASB's projects have been based upon a new conceptual framework which assigns to accounting an increased role in the evaluation of the worth of the entity to the detriment of a realistic measure of performance. This has been done without any preceding debate and without the support of the principal users, including, moreover, the entire investors group. This potentially fundamental revision of the conceptual Framework ought to have been clearly and publicly identified and submitted for approval to the Trustees only once it had been validated by the majority of the stakeholders.

- **Oversight over the respect of the letter and the spirit of the "due process" procedure, over the way that responses to invitations to comment are taken into account and over the rationale behind the decisions ultimately made by the IASB.**

➢ **The IASB**'s independence in the technical domain must be guaranteed. The composition of the Board must be balanced in terms of competence (with a balance between the financial and non-financial sectors) and in its representation of the stakeholders. Once, after appropriate public consultation, the Trustees have confirmed the objectives, the conceptual Framework and the major principles, the Board should ensure that these are put into practice in its standard-setting and be accountable for its work to the Trustees. In particular, the Board should lay out clearly for each project for a new or revised standard the major direction of the project, the objectives of the changes, the reason why these changes are necessary and the principles that will be developed. The IASB staff should play a supporting role (and not a decision-taking role) and that of translating the directions given by the Board into concrete proposals.

<u>**Process: how should the organisation best ensure that its standards are high quality, meet the requirements of a well functioning capital market and are implemented consistently across the world?**</u>

5. Is the standard-setting process currently in place structured in such a way to ensure the quality of the standards and appropriate priorities for the IASB work programme?

Thestandard setting process has to be significantly improved:

➢ The work on the modification of the conceptual Framework should be carried out before the standard setting and not in parallel. The generalisation of concepts which are both vague and changing, such as the balance-sheet approach and "fair value", which are supposed to be derived from the conceptual Framework but have never been dealt with properly in that context, have, in our view, been very detrimental to the quality of recent standards. This has created a major obstacle to their acceptance by the concerned entities.

- Once work on a standard has been completed, it is necessary for an independent quality-assurance review to be performed in order to ensure that the standard actually meets the objectives identified. This role could be given to the Advisory Council.

- The procedure for carrying out impact studies and the way these are taken into account prior to the adoption of new standards should be formalised. Moreover, post-adoption impact appraisal should be obligatory.

- The quality of standards rests largely on their usefulness to entities on a practical, daily basis and on their consistency with financial practice currently in force. The satisfaction of the financial markets with the standards relies on the consistency of the management information of the entity and the information provided to the markets. Accounting standards which are based on theory without being confronted with the economic reality of the entity's business model and are therefore rejected by the management of the entity lead to the proliferation of "non-GAAP" measures. This is damaging to the usefulness of the information provided to the markets.

- Finally, given the deadline of 2011 set in the context of the G20 meetings for the convergence between IFRS and US GAAP, the process followed by the IASB and the FASB, which consists of the revision of the Framework and major overhauls of certain key accounting standards, is detrimental to the quality of accounting standards :

  - It does not correspond to the priorities of investors or entities, who are faced with a certain number of problems with existing standards. Modifications or additions to these standards are very pressing, whereas all the IASB's resources are dedicated to the "convergence" projects;

  - The projects which are a priority for convergence are resulting in a considerable increase in complexity in the standards, leading to significant increases in the cost of producing the information, while there does not appear to be a corresponding increase in the usefulness of the information for users, whether they be investors or the management of the entities.

  - Furthermore, leaving aside these questions of substance, the timetables set for the completion of a set of standards which will fundamentally change the current accounting paradigm are completely unrealistic and incompatible with the objective of producing standards of high quality.

  From the point of view of ACTEO/MEDEF, the objective of useful and consistent standards described above should become the priority, while convergence should be a medium-term aim. In view of the importance of the US financial markets and the level of sophistication of US GAAP, it is inconceivable that major differences could be allowed to survive in the long term between the two accounting paradigms without clear justification.

6. ***Will the IASB need to pay greater attention to issues related to the consistent application and implementation issues as the standards are adopted and implemented on a global basis?***

   Consistent implementation and application of IFRS across the world are dependent on the proper functioning of the current processes which are already in place, at all the different levels:

   Firstly, the prerequisite is a set of high-quality standards, based on robust and well-understood principles that should be applied to all transactions, across all jurisdictions. The IASB should refrain from complementing these principles with too many rules and prescriptive guidance, which give rise to implementational and interpretational difficulties and divergence.

   Secondly, EFRAG, in its endorsement process should advise the European Commission on the quality of these standards, and provide it with assurance that the underlying principles meet the needs of European stakeholders and are capable of being properly applied in a European context.

   Thirdly, even when standards are of high quality, some divergence of practice will probably be observed across jurisdictions. In these cases, IFRIC should be charged with clarifying or interpreting the principle and ensuring that it can be applied to all transactions uniformly, and consistently.

   Fourthly, if a specific and narrow issue is observed in a particular jurisdiction, then the national standard setter should be requested to take up the issue and give its opinion about application of the standard in such a specific circumstance.

   The national standard setters, as well as EFRAG, preparers, and all other stakeholders, should also be actively encouraged to relay information to assist IASB in its debate at a very early stage in the standard's development process.

<u>Financing: how should the organisation best ensure forms of financing that permit it to operate effectively and efficiently?</u>

7. ***Is there a way, possibly as part of a governance reform, to ensure more automaticity of financing?***

   Financing should be provided by all categories of user, including national standard setters and financial regulators in those states which have adopted IFRS. It should be conditional for the participation of a country or an entity to the standardisation process.

   The current situation is not satisfactory as the bulk of the financing is provided by reporting entities, who have no alternative and no guarantee that their views will be properly taken into account. The IFRS Foundation should envisage the creation of a system of automatic financing by all stakeholders. However, this will be possible only if the system of governance is reviewed in depth and accepted by stakeholders.

Other issues

8. Are there any other issues that the Trustees should consider?

The question of who can vote for the adoption of a standard is crucial. It is an anomaly that under the current arrangements, jurisdictions which have not adopted IFRS have greater weight than those representatives of countries whose entities are faced with applying IFRS on a daily basis. This could easily lead to distortions in competition. Beside it is a question of incentive to adopt IFRS. Last but not least, an experience of practical questions posed by the application of IFRS should be required for the board members.

This is a very important issue which must not be ignored nor its resolution delayed.

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