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**IFRS, DO THEY BRING SUFFICIENT
TRANSPARENCY?**

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**IFRS, AS INTRODUCED
IN 2005, DO THEY BRING
SUFFICIENT TRANSPARENCY?**

IFRS: the promise of transparency and comparability for the benefit of investors around the globe

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Introduction

A truly global set of high-quality accounting standards is now within reach for capital markets around the world. The very purpose of disclosure – transparency to investors – requires a language that investors can readily interpret in order to compare and contrast investment options in today's global markets. So long as they are in fact high-quality, comprehensive in scope, and rigorously applied, a single set of global accounting standards offers great promise for improving investor confidence in corporate disclosure by serving as a truly international language of transparency.

The rapidly increasing acceptance around the world of International Financial Reporting Standards reflects a growing consensus that IFRS are in fact the realization of the global accounting standards that so many have advocated and sought for so long. The standards have benefited from the lessons garnered over the past century in the development and application of numerous national accounting standards. They also benefit from having brought to bear the collective wisdom and experience of some of the accounting industry's brightest minds. Even so, because of the relatively limited history of their implementation and interpretation, they will continue to be improved.

Fulfilling the promise of IFRS for consumers of financial information will depend upon continued success in each of the following areas:

- (1) Further enhancements to IFRS to benefit investors;*
- (2) A transparent standard-setting process;*
- (3) An independent standard-setter;*
- (4) Accountability to investor interests and national authorities; and*
- (5) Consistent application across all jurisdictions.*

Investor interest is paramount

The overarching philosophy behind the development of IFRS is and must remain the best interests of current and potential investors. From the investor's standpoint, accounting standards should promote clarity in terms of both understanding an issuer's performance and financial condition, and comparing its financial results and condition with other companies.

These objectives for IFRS are also being driven by the increasingly worldwide acceptance of a global computer language for presenting and comparing financial information. The International Accounting Standards Committee Foundation has aggressively supported the international movement to employ eXtensible Business Reporting Language through its annual publication of the IFRS taxonomy. This is a very welcome development. The widespread use of XBRL to publish IFRS financial information would be useful to investors since it would enable investors to download IFRS information directly into spreadsheets, analyze it using commercial off-the-shelf software, and use it within investment models in a variety of software formats. This will enhance the inherent potential of IFRS to aid in the comparison of financial information between companies and across industries.

Discussion should also center on whether there are additional means for ensuring that investors' interests remain the primary concern in the continued development of IFRS. This is particularly pertinent today, amidst discussions of fair-value accounting, consolidation of off-balance sheet items, and other hot-button issues that have come to the fore during the recent period of market turmoil.

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Transparency in standard setting

For investors to have full confidence in a set of accounting standards, they must believe that the standard-setting process was conducted in a fully transparent manner. This means that the process for developing accounting standards should allow for input from all affected parties. And, in finalizing its standards, the standard setter should reveal clearly what substantive views it adopted, those it rejected, and its rationale for doing so.

The IASB has instituted a number of procedures to incorporate transparency into its standard-setting process. The IASB solicits views and seeks input from its constituents throughout the standard-setting process – from selecting items for its agenda, to developing and publishing an exposure draft, to issuing a final standard. In addition, the IASB's meetings are open to public observers. The IASB also makes public on its website the comment letters it receives, as well as staff papers that summarize comments received on discussion papers and exposure drafts, soliciting public comment on any proposed new standards or changes to existing standards.

Many countries incorporate the notion of transparent regulatory procedures into their regulatory rule-making processes. Moreover, procedures designed to promote transparency – including public consultation, minimum consultation periods, and publication in advance of a standard becoming effective so that users can become familiar with it – are incorporated into trade agreements, as well as compilations of best practices in the area of administrative procedures, due to their importance in promoting workable standards and guidelines.

For securities regulators, IFRS is perhaps the first true exercise in establishing globalized standards having a direct and immediate impact within individual nations. This places a high premium on ensuring that the standard-setting process is accessible to a worldwide user group. The improvements already made to the IASB's transparency procedures give reason to be confident that additional transparency enhancements will continue to be introduced.

Independence as insulation from political pressures

Two other key characteristics of a global accounting standard setter are that it should be independent and professional. This means that the standard setter should not be subject to undue funding pressures, or made dependent upon political or corporate largesse. The individuals who lead the standard setter should be chosen for their professional competence. In addition, while geographic diversity is necessary to ensure that vital expertise from different regions is reflected in the standards-setting process, members of the standard setter should not be chosen on the basis of specific national interests or political representation. This would undermine investor confidence in IFRS. All of us have a strong interest in upholding the independence and professionalism of the IASB as a standard setter, because this is the sine qua non of high quality standards.

The IASB is overseen by the IASC Foundation, a stand-alone organization responsible for, among other things, the activities of the IASB. The 22 trustees of the IASC Foundation appoint IASB members, and oversee the activities of the IASB, the IASC Foundation, the International Financial Reporting Interpretations Committee, and the Standards Advisory Council. The IASC Foundation Trustees select members of the IASB to comprise “within that group, the best available combination of technical skills and background experience of relevant international business and market conditions in order to contribute to the development of high-quality, global accounting standards.” The fourteen members of the IASB are required to sever all employment relationships and positions that may give rise to economic incentives which might compromise a member's independent judgment in setting accounting standards. The IASB thus operates on a stand-alone basis and has professional members.

With respect to funding, the IASC Foundation Trustees continue to make progress on establishing their independence. For now, the IASB's funding is still largely derived from ad hoc donations by various stakeholders. Each of us will have to work together to assist the IASC Foundation and the IASB in establishing a global, independent, sustainable and consistent source of funding that will undergird the independence of the accounting standard setter.

Accountability

Just as rights carry correlative responsibilities, so standard-setting independence implies accountability for maintenance of high standards, transparency in rulemaking, and fidelity to investor interests. This is particularly so since national authorities responsible for establishing the accounting standards to be used in a given jurisdiction already have (or will, by virtue of their adoption of IFRS) invested their confidence in a global standard setting process. The SEC, for example, now allows foreign private issuers to prepare their financial statements according to IFRS as issued by the IASB, without reconciliation to US Generally Accepted Accounting Principles. Other jurisdictions have gone further by mandating the use of IFRS for all issuers. This is undeniably a significant step in the globalization of capital markets, but it requires that we who are most directly charged with representing investors' interests continue energetically to insist that IFRS in fact creates a common accounting language of transparency that stems from a transparent and independent process.

In that context, I note that the IASC Foundation is explicitly dedicated to the development, in the public interest, of a single set of high-quality, understandable and enforceable accounting standards. This public interest mandate is written into the IASC Foundation Constitution. Upon their appointment, all Trustees must formally commit to acting in the public interest in all matters.

To further enhance this public interest focus and strengthen the institutional framework of the IASC Foundation, last November the SEC, Japan Financial Services Agency, European Commission, and IOSCO announced our work plans to contribute to strengthening the governance structure of the IASC Foundation. This will take the form of a new monitoring body to which the IASC Foundation Trustees would report, and which would participate in the appointment of new Trustees. This new governance structure will affect only the IASC Foundation, and not the IASB, as a further protection of the independence of the IASB.

The new monitoring body was conceived to address the need to ensure the accountability of a global accounting standards setter in a world where national authorities retain final jurisdiction over financial reporting. The charter of the new monitoring body would be to preserve the independence of the IASB. In this way, both preserving the independence of the IASB and promoting the accountability of the IASC Foundation to national authorities can be thought of as mutually reinforcing objectives, both serving the interests of investor protection.

Cooperation as the foundation

The current dialogue among financial regulators regarding IFRS development should also continue to promote consistency in application. The development of IFRS as a uniform global standard and the goal of comparability for investors worldwide require that we cooperate to head off any incipient tendency toward the dissolution of IFRS into a divergent set of standards applied differently in every nation. Consistency of application of IFRS will help investors who increasingly trade securities outside of their home markets to better understand and compare their investment options – and to do so far better than they ever could with the multiplicity of national accounting standards that existed before the introduction of IFRS.

That is why the ongoing dialogue among issuers, auditors, standard setters and regulators about the various implementation and application issues they encounter is so critical. Through this process, each stakeholder can learn from the others' experiences. In addition, referral of interpretive matters to the IASB's interpretive body, the International Financial Reporting Interpretations Committee, will promote both consistency in application and improvements to the standards themselves.

For regulators, achieving the goal of consistency in application will require a new degree of coordination. IOSCO has shown leadership in this respect by creating a database for use by securities regulators to catalogue and share securities regulators' experiences on IFRS application around the world. On a bilateral basis, the SEC and the Committee of European Securities Regulators have put into action a work plan covering information sharing regarding the application of IFRS, as well as the confidential exchange of issuer-specific information between CESR members and the Commission through implementing protocols. As we continue our important collaboration on the use of IFRS, we will need to redouble our efforts to develop additional mechanisms to promote consistency and avoid conflicting decisions on IFRS application matters.

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Conclusion

As IFRS sweeps the world, the ultimate question – whether it becomes the single set of high-quality, global accounting standards – will depend on investors' confidence in the reliability, transparency, and comparability of the financial information that those standards produce. Ensuring a transparent and independent standard-setting process is critical to setting the stage for the further development of international accounting standards in the best interests of investors. At the same time, the investor protection mandate for global accounting standards requires that the standard-setter be accountable to those charged with investor protection in individual jurisdictions. Finally, the investor protection objectives of reliability, transparency, and comparability can only be achieved if IFRS is applied and interpreted consistently across all industries and jurisdictions. The challenge for regulators is to find mechanisms to promote these objectives simultaneously, all the while keeping investors' interests absolutely paramount.