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Organización Internacional de Comisiones de Valores
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Organização Internacional das Comissões de Valore

December 14, 2006

Ms. Li Li Lian
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International Accounting Standards Board
30 Cannon Street
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Dear Ms. Lian:

The International Organization of Securities Commissions (IOSCO) Standing Committee No. 1 on Multinational Disclosure and Accounting (Standing Committee No. 1 or SC1) thanks you for the opportunity to provide our thoughts regarding the International Accounting Standards Board (IASB or the Board)'s Discussion Paper: *Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting Information* (the Discussion Paper or the Paper).

IOSCO is committed to promoting the integrity of international markets through promotion of high quality accounting standards, including rigorous application and enforcement. Members of Standing Committee No. 1 seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein reflect a general consensus among the members of Standing Committee No. 1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

General Comments

Scope of the Framework

The scope of the Discussion Paper addresses *financial reporting*, while the scope of the existing IASB framework is limited to *financial statements*. In paragraph BC1.4 of the Basis for Conclusions, the Boards do not indicate why they believe it is appropriate at this time to make the scope broad enough to encompass *financial reporting*. Is this based upon a line of reasoning that concludes that the objective and qualitative characteristics of the information provided would be the same regardless of whether the scope was financial reporting or financial statements? Or is it based upon studies of evidence to that effect? SC 1 is not aware of any studies to that effect. In either event, the basis for this conclusion is not clear, and leads us to ask, would it be more practical to focus on objectives of *financial statements* at

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this stage of development? Subsequently, the Board could consider how the Framework's objectives could be extended to other aspects of *financial reporting*.

The objective of financial reporting

First and foremost the Board should determine whether the scope of the Framework is focused on *financial reporting* or *financial statements*. This is necessary because this distinction may engender differing views about the nature of the objective or objectives needed to serve those respective ends.

Under either scope we agree, as stated in paragraph OB2, that an objective of "general purpose external financial reporting is to provide information that is useful to present and potential investors and creditors and others in making investment, credit and similar resource allocation decisions." The question is whether this is *the* objective under either scope alternative.

In thinking about this question it is worth considering precisely the decisions that a security holder or potential security holder makes. These decisions seem to fall into the following categories; (i) whether to buy, hold or sell an investment and, in the case of a security with voting rights, (ii) how to cast votes during the time that securities are held.

While we can appreciate an argument that the information needed to make voting decisions may not be found *entirely* in the *financial statements*, (for example, auditors fees and management compensation), it is difficult to believe that none of this information could be derived from the broader concept of *financial reporting*. Further, understanding that the *stated scope* of the Discussion Paper encompasses the broader concept of *financial reporting*, the existence of the voting decision begs the question as to what is the source of the information on which the decision makers will base their conclusions. Is it from the information derived from financial statements or financial reporting? The Discussion Paper acknowledges (paragraphs OB 27 and 28) that some may view voting as an action separate from deciding whether to buy, hold or sell a security, but it ultimately asserts that those information requirements are still encompassed in the stated objective. However, it stops short on providing a clear analysis of how the information necessary to vote on matters is inherently included in the context of *financial reporting*.

In the context of *financial reporting*, if the Boards believe the decision of how to vote is a process inherent in the decision to buy, hold or sell that security, similar to determining how much of a security to buy or sell would be, then we suggest that the Framework amplify how its stated objective inherently includes providing all information useful to investors, including the additional information necessary to make decisions on how to vote.

Stewardship

SC1 members agree that financial reporting information about the future cash flows of an entity is important in helping investors make decisions. All members also agree that information about how management utilized the entity's resources is an important aspect of financial reporting because that information is one indicator (although not the only indicator) of how management might use the entity's resources in the future. This is information that in turn helps investors in making all of their decisions. What is not entirely clear to all SC1 members is whether both types of information can be encompassed by the Discussion Paper's *single* financial reporting objective.

Some members of SC1 share the view, expressed in the Alternative View section of the paper (see paragraphs AV1.1-1.7), that stewardship should be identified as a separate objective of financial statements. Those members assert that, in many jurisdictions, stewardship and accountability (henceforth 'stewardship') were initially the primary reasons why financial statements were prepared. Those members believe that the subsequent development of capital markets has meant that there is now another reason for preparing financial statements, but the stewardship objective remains. Further, those members believe that the suggestion that the stewardship objective is nothing more than a subset of the resource allocation decision-usefulness objective takes too narrow a view of the information that can be needed to assess stewardship. An example of this is the way the Framework equates the resource allocation decision-usefulness objective with the need to provide information that helps in assessing the amount, timing and uncertainty of the entity's future cash flows (paragraphs OB3 and OB13); these members of SC1 believe the stewardship objective cannot be met simply by providing information that helps in assessing future cash flows.

Other member(s) of SC1 are not yet convinced that stewardship should be a separate objective of financial statements. Initially, there is a question as to how the nature of a stewardship objective maps to the nature of an objective designed to inform, as appropriate, the types of decision making by current and potential security holders [(i) buy, sell, hold and (ii) voting], in the context of a financial statement scope. Further, there is a question as to whether the nature of the information needed to serve a stewardship objective differs from the nature of the information needed to serve those same two types of decisions.

Conflicts between the Framework and future financial reporting standards

We understand that creating and maintaining financial reporting standards is an evolving process. While the IASB should strive to develop new standards that are consistent with the existing Framework (as amended through its current project), we understand that doing so may not always be possible. In developing future standards, the IASB may decide that it is appropriate to diverge from the Framework. The Discussion Paper's paragraph IN 5 acknowledges this point; however, it does not provide for a process whereby the IASB would, as a result, consider whether the reason for a diversion indicates that it would be appropriate to amend the Framework. We believe the Board should include a discussion in the Framework about its commitment and its related process necessary to consider whether it is appropriate to amend the Framework in circumstances when the Board issues a new standard that is inconsistent with the existing framework. If the Framework is not amended timely, there is a risk that it will lose its usefulness.

Faithful representation

The Paper explains that the Board is proposing to elevate *faithful representation* as a qualitative characteristic of financial reporting information to replace the term *reliability* that is used in the current Framework. We understand the Board's desire to eliminate confusion among constituents previously generated by use of the term *reliability*. However, we do not believe the Board has been sufficiently persuasive as to why use of the term *faithful representation* will improve constituents' understanding. While we do not have a specific recommendation for a term to replace *reliability*, we believe the Board should further explore the reasons for past confusion over the term *reliability* and further consider whether the discussion of *faithful representation* will be understandable to most constituents. Although *faithful representation* is not a new term in the Framework, it is not necessarily a "plain English" term and may need to be reconsidered. In particular, the Discussion Paper does not explain the reason for the modifier *faithful* preceding the term *representation*. What other types of representation are there? How could something be *unfaithful* and still be *representational*? Is the term *representational* adequate?

SC1 believes that *substance over form* is an important qualitative characteristic of financial reporting information. Our members that have experience with the application of IFRS have found that the discussion in the current Framework of *substance over form* separate from the discussion of *faithful representation* has been helpful in applying IFRS. Those members do not believe the Framework is improved if it asserts that the inclusion of *substance over form* as a separate qualitative characteristic is unnecessary or redundant.

Other detailed comments are presented in an attachment to this letter.

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We appreciate your thoughtful consideration of the comments raised in this letter. If you have any questions or need additional information on the recommendations and comments that we have provided, please do not hesitate to contact me at 202-551-5300.

Sincerely,

Scott A. Taub

Scott A. Taub
Chairman
Standing Committee No. 1

ATTACHMENT

Developing the Framework/Introduction to Chapter 1

Paragraphs P8, OB 1 – The Paper states that: "The first chapter of the [draft] conceptual framework establishes the objective of general purpose financial reporting by business entities in the private sector." We understand that the term "private sector" has differing meanings in different jurisdictions. In some jurisdictions, "private sector" refers to those entities that do not have publicly traded debt and/or equity securities, where as in other jurisdictions it may mean non-governmental entities. To avoid confusion, we suggest providing further clarification of the intended meaning of "private sector".

Shareholder perspective vs. Entity perspective

Paragraph OB10 - The Paper asserts that financial information should be directed to the needs of a wide range of users, rather than to the needs of a single group and therefore is premised on an entity perspective rather than a shareholder perspective. However, the Paper does not provide a full analysis of why financial information designed to satisfy the needs of a wide range of users under an entity perspective is the more appropriate perspective in the context of other areas. For example, there is little discussion of the impact the entity perspective has on competing notions of the definition of a business entity or the financial reporting effects of selected accounting decisions. Therefore, we suggest the Boards consider further and perhaps include more discussion on the impact of an entity perspective.

Potential users of financial reports and their information needs

Paragraph OB 6 – We suggest changing the last sentence of the paragraph to read: "Potential users of financial reports and their information needs ***may*** include:" as the list of users is not necessarily comprehensive.

Economic resources and claims to them

Paragraph OB 20 – The Paper states that "... financial reports are not designed to show the value of an entity." This fact is important and we suggest that it be more prominently displayed by moving this sentence to paragraph OB 2 thereby highlighting what the objectives for financial reporting are and what they are not.

Financial performance measured by accrual accounting

Paragraph OB 23 – The Paper states: "Therefore, information about financial performance measured by accrual accounting rather than only by the entity's cash transactions ...is essential to users of financial reports..." It is unclear how accrual accounting relates to the notion of measurement. Accrual accounting is generally regarded as a recognition notion. If the document intends to discuss measurement, we suggest including discussion about fair value, historical cost, and other measurement bases.

Understandability

Paragraph QC 40 - The first sentence states: "Information cannot influence a particular user's decision unless it is presented in a manner that the user can understand." This is not necessarily a factual statement. Certain investors may attach a risk premium (discount) to the price of securities if financial information is not understood. Those users then are, indeed, influenced by the information provided specifically because it is not understood. While we appreciate the example given in paragraph 40, we would suggest eliminating the first sentence of the paragraph. At worst, the sentence contradicts the example given and, at best, adds no value.

General

The practice of using bold-faced comments throughout the document seems unnecessary and confusing. In the final document we suggest using bold-faced font only for titles and sub-titles within the Paper.