

The Chairman

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**IFRS Foundation
Monitoring Board
Mr. Masamichi Kono
Acting Chairman**

**c/o Japan Financial Services
Agency
3-2-1 Kasumigaseki Chiyodaku
Tokyo 100-8967
Japan**

IFRS Foundation Monitoring Board Consultative Report on the Review of the IFRS Foundation's Governance

Dear Mr Kono,

The European Securities and Markets Authority (ESMA) is an independent EU Authority that contributes to safeguarding the stability of the European Union's financial system by ensuring the integrity, transparency, efficiency and orderly functioning of securities markets, as well as by enhancing investor protection.

The Monitoring Board of the IFRS Foundation published on 7 February 2011 its *Consultative Report on the Review of the IFRS Foundation's Governance*. We thank you for this opportunity to comment on the IFRS Monitoring Board's proposals on the review of the IFRS Foundation's governance.

ESMA fully shares the view that the fundamental question for the review is whether the current governance structure effectively promotes the standard-setter's primary mission of setting high quality, globally accepted standards as set forth in the IFRS Foundation's Constitution. We believe that this can best be achieved through building further on the existing governance structure comprising three levels whereby the IASB is overseen by the IFRS Foundation which in turn is overseen by the Monitoring Board, representing public authorities.

We however believe that there is room for improvement in the composition and functioning of the Monitoring Board as the first-tier body in the near term. We acknowledge the important role of the European Commission in the area of financial reporting in the EU and strongly support its membership of the Monitoring Board. At the same time ESMA believes that, as the representative of enforcers of IFRS and securi-

ties regulators of by far the largest economic area and the highest number of entities applying IFRS, it should be part of the Monitoring Board alongside the European Commission, at least as an observer because its experience would add considerable value to the activities of the Monitoring Board. We believe that a similar need for accepting two representatives, possibly with a single vote, may arise in other jurisdictions that could in the future become members of the Monitoring Board.

Our detailed comments are set out in the appendix to this letter but to highlight some:

— *On the Trustees*

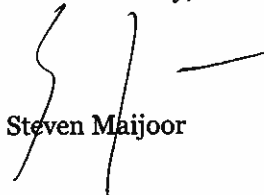
We appreciate the Trustees' efforts, particularly in the field of securing funding and improved oversight. However, the IFRS Foundation needs to be seen to be exercising its governance and oversight role actively if it is to be effective. The IFRS Foundation's role should be a pro-active one, acting on the organisation's behalf to work with jurisdictions to ensure their support of (or non-interference with) the standard-setting process and promoting the use and adoption of IFRSs. The IFRS Foundation should act as a buffer between the independent standard-setter and the Monitoring Board members and other parties representing jurisdictional interests. This implies a more visible role for the Trustees than at present in the governance and oversight of the IFRS Foundation and a visibly ambassadorial role for them liaising with policy-makers in IFRS jurisdictions and potential IFRS jurisdictions, ensuring that lines of communication remain open and accessible to the IASB.

— *On the IASB*

In general, we believe that that the IASB is a transparent organisation and has made significant steps in developing its outreach programme to ensure that stakeholder views are taken into account during the standard-setting process. The organisation should develop this further by dedicating sufficient resources to understanding the impact of proposals prior to the issuance of Exposure Drafts, including assessing (for example, through robust market failure analysis or cost-benefit analysis), the need for any such proposals, giving greater consideration to the number of amendments that users and preparers of financial information can reasonably absorb within certain time frames, issuing more formalised feedback statements and carrying out more systematic post-implementation reviews.

I would be happy to discuss all or any of these issues further with you.

Yours sincerely,



Steven Maijoor

APPENDIX – ESMA’S DETAILED COMMENTS ON THE QUESTIONS ASKED IN THE CONSULTATIVE REPORT

Question 1

Do you agree with the proposal to urge concrete efforts to deepen the pool of candidates for IASB membership from diverse geographical and professional backgrounds? Please provide reasons for your agreement/disagreement.

1. ESMA believes that the composition of the IASB should foremost be such that the IASB can fulfil the IFRS Foundation’s mission to ‘*develop, in the public interest, a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles*’. The composition of the IASB should be a matter primarily for the Trustees. However, like the Monitoring Board we believe that members should be drawn from the broadest possible geographies and professional backgrounds representing IFRS’s diverse stakeholders and that more effort is needed to achieve this goal when identifying and selecting (potential) candidates. This diversity should however not be pursued at the expense of technical expertise. Further increases in the size of the IASB might make it less efficient.
2. The Constitution sets out that a Board member should fulfil certain criteria including demonstration of technical competence and knowledge of financial accounting and reporting, whilst at the same time prescribing a distribution across geographic areas. Although the two are not completely incompatible, it seems that, in practice, geographic representation has been a stronger driver than technical expertise. Although both approaches have merit, we believe that there needs to be a clear – and clearly articulated – choice between whether the primary consideration for the composition of the Board is geographic representation or technical expertise, because this choice would impact:
 - The depth of the pool of candidates for Board membership;
 - The role and responsibilities of Board members, making part-time membership a more or less likely membership model; and
 - The role and responsibilities of the IASB staff, potentially requiring a reassessment of IASB staff’s profile and technical expertise.
3. We agree with the Monitoring Board that the process for identifying technically qualified candidates for IASB membership could be improved and that more promotion is necessary. In addition, we believe that there is a need for the Trustees to communicate more clearly on the due process that has been applied to the selection of Board members. We believe that this should be possible without harming the confidentiality that candidates might require.

Question 2

Do you agree with the proposal to separate the roles of the IASB Chair and the CEO of the IFRS Foundation, and if so would you have suggestions on how to formalize? Please provide reasons for your agreement/disagreement.

4. Although we agree that the past model of combining the two roles has to a certain extent provided a bridge between the standard-setter and its governing body, we are supportive of now separating out the roles of the IASB Chair and the CEO of the IFRS Foundation. We believe that the structure of a Chairman/CEO worked in the smaller organisational structure of the International Accounting Standards Council Foundation (IASCF) at its inception but that this structure no longer matches the current expectations of the Foundation. Both the fact that more than one hundred jurisdictions worldwide either use or are in the process of adopting IFRSs and the nature of the future work plan make us believe that the chairmanship of the IASB is a full-time position. In addition, we agree that separating the two functions out would enhance the governance structure of the Foundation by eliminating possible risks of conflicts of interest between the overseer and the subject of the oversight.

Question 3

Do you agree that clearer division of responsibility between staff dedicated to the IASB operations and staff dedicated to the Foundation's administrative and oversight functions should be considered, and if so, would you have suggestions how to formalize this? Please provide reasons for your agreement/disagreement.

5. Safeguarding the independence of the standard-setting process and avoiding real or apparent conflicts of interest is important for ESMA and as set out in our response to question 2 we are supportive of separating the roles of the chair of the IASB and the CEO.
6. ESMA is also supportive of dedicated secretariat resources for the Trustees to support their oversight of the IASB, particularly if the Trustees are to become more active in this function. In other words, we believe that allocating secretariat resources to the Trustees would enhance their ability to effectively monitor the IASB's non-technical decisions and challenge the IASB where necessary.
7. We are not however convinced that the Monitoring Board should intervene in the organisation of the staff. This should be the responsibility of the CEO in liaison with the Trustees to prevent formalising the structure too much.

Question 4

Please provide comments on any aspects of Trustee composition or appointments that you believe the Monitoring Board should consider.

8. The IFRS Foundation needs to be seen to be exercising its governance and oversight role actively if it is to be effective. The IFRS Foundation's role should be a pro-active one, acting on the organisation's behalf to work with jurisdictions to ensure their support of (or non-interference with) the standard-setting process and promoting the use or adoption of IFRSs. The IFRS Foundation should act as a buffer between the independent standard-setter and the members of the Monitoring Board and other parties representing jurisdictional interests. This implies a more visible role for the Trustees than at present in the governance and oversight of the IFRS Foundation and a visibly ambassadorial role for them liaising with policy-makers in IFRS jurisdictions and potential IFRS jurisdictions, ensuring that lines of communication remain open and accessible to the IASB. Such contacts could include governments, those responsible for incorporating/endorsing IFRS for use in their jurisdictions and those responsible for the enforcement of the standards in those jurisdictions.
9. ESMA has always been supportive of the Trustees' efforts to ensure an appropriate balance of professional backgrounds within the Trustees as a group whilst respecting an appropriate geographical distribution in their places of origin. We support the intent of the Monitoring Board to consider appropriate diversity as part of the approval process whilst preserving the quality of the Trustees. In that respect we believe that it is important that all Trustees should be able to dedicate sufficient time to fulfilling their obligations as Trustees and to meeting the expectations that exist of them. Given the heightened profile of the IFRS Foundation now as a result of the G20 mandate given to the IASB, we see this requirement as unavoidable. In addition, we believe that the recruitment process for Trustees should be broadened and more publicity should be sought for vacancies than is currently the case.
10. Where the IASB has made significant progress towards becoming a more transparent organisation is in developing its outreach programme to ensure that stakeholders' views are taken into account during the standard-setting process, but there is still a long way to go for Trustees. The Trustees should strengthen their oversight activities, promote more transparency and better communicate with their stakeholders. One particular area where such transparency and communication could be improved is on the activities of the Due Process Oversight Committee.

Question 5

- **Do you agree with the proposal to provide increase transparency into the process for Trustee nominations? Please provide reasons for your agreement/disagreement. To what extent should the Monitoring Board be involved in the nomination process?**

— **Do you agree that further clarification of criteria for Trustees’ candidacy would help support confidence of the stakeholders? Please provide reasons for your agreement/disagreement.**

11. We share the Monitoring Board’s concern that the processes around how the Trustees are recruited, selected and nominated is not clear for those not directly involved. We would welcome the suggestion of documenting and publishing formal procedures for the nomination of Trustees, including clear criteria for candidacy.
12. We believe that there is not only a need for more transparency regarding the process of Trustee nominations but that it would be beneficial if the Monitoring Board and the Trustees could clarify how duties and responsibilities are divided between them.
13. We also recommend that the Due Process Oversight Committee should increase its responsibilities to safeguard the IASB’s independence and ensuring the IASB is accountable. In our view, the IFRS Foundation Constitution should be amended to explicitly mention the Due Process Oversight Committee’s role in the IASB’s due process, so as to enable the Committee to meet with the IASB upon request, and to give it the explicit obligation to assess the way the IASB complies with the Due Process Handbook for the IASB. The Committee should report on these activities and on its conclusions to the Monitoring Board and to the wider public on behalf of the Trustees.
14. As further discussed in question 12, a significant part of the funding of the Foundation is voluntary and therefore unstable; we believe that it could enhance the transparency of the Foundation if it would disclose the funding it receives from any organisation to which a member of Trustees belongs or which is dependent on the funder obtaining or retaining membership of the Trustees.

Question 6

- **Should the membership of the Monitoring Board continue to be confined to capital markets authorities responsible for setting the form and content of financial reporting in respective jurisdictions?**
- **Do you agree with the proposal to expand the Monitoring Board’s membership by adding a mix of permanent members ([four]) representing primarily major emerging markets and rotating members ([two]) from all other markets? Please provide reasons for your agreement/disagreement. How should the major markets be selected? Should a jurisdiction’s application of IFRS and financial contribution to standard-setting play a role?**
- **Do you agree that rotating members should be selected through IOSCO? Please provide reasons for your agreement/disagreement?**

15. The primary purpose of the Monitoring Board is to serve as a mechanism for formal interaction between capital markets authorities and the IFRS Foundation, thereby facilitating the ability of capital markets authorities that allow or require the use of IFRS in their jurisdictions to effectively discharge their mandates relating to investor protection, market integrity and capital formation. Under the current governance structure, primary roles and responsibilities borne by the Monitoring Board include: (a) participating in the Trustee nomination process and approving Trustee nominees; (b) reviewing the adequacy and appropriateness of the Trustee arrangements for financing the IASB; (c) reviewing the Trustees' oversight of the IASB's standard-setting process; (d) conferring with the Trustees regarding their responsibilities, in particular in relation to regulatory, legal and policy developments; and (e) referring to the Trustees matters of broad public interests related to financial reporting.
16. Against this background we believe that the Monitoring Board should be composed mainly of public oversight bodies responsible for regulating and enforcing transparency in capital markets. ESMA fully shares the Monitoring Board's recommendation that its composition should be enhanced, particularly with more representatives from emerging markets. A jurisdiction's commitment to adopting IFRS within a reasonable timeframe and a composition reflecting market capitalisation are in our opinion key criteria for the composition of the Monitoring Board and thus for selecting its members.
17. Against this background, ESMA believes however that it would enhance the public accountability of both the Foundation and the Monitoring Board if it would be possible for jurisdictions where there is more than one relevant authority to nominate a second representative as an observer. Although ESMA acknowledges the important role of the European Commission in the area of financial reporting in the EU and its membership of the Monitoring Board, ESMA believes that, as enforcers of IFRS and securities regulators of by far the largest economic area and the highest number of entities applying IFRS, it should be part of the Monitoring Board alongside the European Commission at least as an observer and that its experience would add considerable value to the activities of the Monitoring Board. We believe that this is also in line with the proposals of the Monitoring Board that members should primarily be drawn from within IOSCO, an organisation representing securities regulators. We believe that a similar need for accepting two representatives, possibly with a single vote, may arise in other jurisdictions that could in the future become members of the Monitoring Board
18. ESMA is not supportive of the idea of setting up an advisory body or other ways of formalising dialogue meetings with important international regulatory stakeholders. If the opinion of these organisations (such as the Financial Stability Board, Basel Committee on Banking Supervision, World

Bank etc.) is considered important, then they should participate at the level of the Monitoring Board albeit as observers.

Question 7

Do you agree that the Monitoring Board should continue to make its decisions by consensus? Please provide reasons for your agreement/disagreement? Are there any types of decisions taken by the Monitoring Board for which voting other than by consensus (for example, by qualified majority) may be appropriate? If so please describe why and suggest an appropriate wording mechanism.

19. ESMA supports continuing with the provisions in the current Charter of making all decisions by consensus. Given the relatively small size of the Monitoring Board and that the role of the Monitoring Board is primarily one of governance, it is unlikely that it will have to deal with issues in emergency situations requiring voting or where achieving a common position is impossible. The introduction of a voting system or holding discussions on the relative weight of the jurisdictions represented might also have knock-on effects on the development of IFRSs which should be avoided.

Question 8

To ensure increased involvement of public authorities and other international organisations in the Monitoring Board activities, do you support the Monitoring Board (a) expanding the number of Monitoring Board observers, (b) holding more formalized dialogue, or (c) establishing an advisory body, and on what basis? What should be the criteria for selecting participants?

20. ESMA thinks that it is important to differentiate between the need for independent high quality execution of standards and the need for a strong accountability framework. The former should help to ensure the latter. We believe that the IASB should improve participation of all relevant stakeholders, including relevant regulatory and supervisory authorities in the standard-setting process. The IASB should organise a forum for technical experts representing securities and prudential regulators to discuss the potential impact on supervision of upcoming standards.
21. In line with our response to question 6 we would prefer expanding the number of Monitoring Board observers to holding more formalised dialogue or establishing advisory bodies. The stakeholders mentioned in the consultative report are important in the international regulatory environment and their views are important for the development of IFRSs. Setting up separate advisory bodies might make the governance framework unwieldy and incapable of responding to new developments.

Question 9

Do you believe that the current arrangements for the standard-setting process adequately ensure the appropriate involvement of all relevant stakeholders and that all relevant public policy objectives are taken into account? Please provide reasons for your agreement/disagreement?

22. For ESMA, preserving the independence of the standard-setter remains key to ensuring its standards are high quality and meet the requirements of well-functioning capital markets. In general, we believe that the IASB is a transparent organisation and has made significant steps in developing its outreach programme to ensure that stakeholder' views are taken into account during the standard-setting process. As we believe that the IASB's technical agenda-setting could be more consultative, we welcome the development that the IASB will begin its deliberations on its future agenda later this year by launching its first triennial public consultation process (as requested by many of its constituents). We hope that this better engagement with stakeholders will avoid in future the extreme congestion in the IASB's agenda that has been the experience recently (even though the IASB has postponed some projects, it will still be challenging for the IASB to complete all the remaining projects within the current deadlines).
23. ESMA believes that the following considerations could lead to further possible improvements in the standard-setting process:
- Greater consideration of the number of amendments to IFRSs that users and preparers of financial information can reasonably absorb within certain time frames. An overload of new accounting standards can affect the proper implementation of standards by preparers;
 - Sufficient allocation of resources to meet market participants and to analyse market failures prior to developing exposure drafts. This will lead to a better assessment of the need for the new proposals and their scope, the identification of unintended consequences and, ultimately, broader acceptance of the legitimacy of the standards that are adopted;
 - Greater formalisation in the process for feedback statements on comments received in public consultations;
 - More widespread use of post-implementation reviews of the major standard-setting projects; and
 - The setting of clearer criteria for re-exposure of exposure drafts.

We believe that both the IASB and the Foundation have made important progress in better involving stakeholders in the standard-setting process. This engagement, particularly with regulatory authorities, should now be placed onto a more structured basis.

Question 10

What are the appropriate means and venues for the Monitoring Board to enhance the visibility and public understanding of its activities?

24. The role of the Monitoring Board – as a link between the Trustees and public authorities – should clearly be to assess to what extent the Trustees, the IASB and other committees within the IFRS Foundation act or have acted in the fulfilment of the public interest. ESMA believes that there is a need for the Monitoring Board to develop the transparency and effectiveness with which it carries out this important role. We agree with the concerns expressed by some stakeholders that disclosure of the public portion of the Monitoring Board meetings through the IOSCO website and provision of agenda papers from meetings with the Trustees on the IFRS Foundation website are insufficient.
25. ESMA believes that there should be a unique website or at least a separately identifiable section in the Foundation's Website for all activities relating to the Monitoring Board. Such a website should include background information, supporting (public) agenda papers and a calendar of upcoming meetings.

Question 11

Do you believe that the current arrangements for Monitoring Board involvement in the IASB's agenda-setting are appropriate, or should the Monitoring Board have an explicit ability to place an item on the agenda, or would you consider other alternatives that would enhance the Monitoring Board involvement in the IASB agenda setting? Please provide reasons.

26. Overall we do not believe that the Monitoring Board should be able to add or remove items from the IASB's agenda. The Monitoring Board should however discuss and approve a general mission statement (and strategic plan) developed by the Trustees on the adoption of IFRS in various jurisdictions, convergence, relationships with national/regional financial reporting bodies and the development of IFRSs – including work agenda and convergence program.
27. The IASB should set its own agenda after appropriate public consultation. Decisions to add items to its agenda should be supported by robust evidence of need, for example through market failure or effect analyses. The role of the Monitoring Board should be to ensure that Trustees fulfil this oversight role effectively.
28. Trustees need however to be actively involved as the IASB identifies candidate projects for its agenda, prioritises them and reviews the feedback received from constituents on that assessment. Although we support the status quo in which the Trustees do not have a detailed involvement in the

IASB's agenda-setting process, Trustees should be more involved to the point that they fully understand the process by which the IASB has determined its agenda and set the relative priorities, such that they can present and explain this process at senior levels. Such involvement should include active engagement with the IFRS Advisory Council, in a session attended by Trustees. The Trustees must be visible in these public fora if they are to be credible in discharging their oversight role.

Question 12

Do you have concrete suggestions on how the Monitoring Board or the Trustees could encourage a move towards a more stable and independent funding model?

29. ESMA believes that the necessary independence of the IASB and the IFRS Foundation could be strengthened by more stable and diversified funding. A stable funding mechanism benefits the IASB by allowing it to carry out its technical agenda and attract high-quality staff. It also provides greater assurance to jurisdictions using or in the process of adopting IFRSs regarding the quality and independent nature of the accounting standards. Sufficient and independent funding is key to achieving this objective.

30. ESMA believes that the Foundation should move as quickly as possible to a funding structure that relies solely on public sponsorship and other intermediated mechanisms – this would exclude reliance on voluntarily contributions. We believe that the different regulators within the jurisdictions using or in the progress of moving to IFRS should further consider developing stable funding mechanisms to fund the IFRS Foundation. We note in this respect that the European Commission has decided recently to contribute to the Foundation and that National Funding Mechanisms have been set up in some European jurisdictions.

Question 13

- **Do you believe that the Monitoring Board should have a more prominent role in the selection of the IASB Chair? Do you agree with the proposal that the role include involvement in establishing a set of publicly disclosed criteria for the Chair, and assessment of a short list of candidates against those criteria? Please provide reasons.**
- **Do you believe that the Monitoring Board should be given any further, specific role in the selection of the IASB Chair? In particular, should the Monitoring Board approve the Trustees' final selection? Please provide reasons.**

Question 14

- **Do you agree that the Monitoring Board's responsibilities should explicitly include consultation with the Trustees as they further develop the framework to ensure proper balance in the composition of the IASB? Please provide reasons for agreement/disagreement.**

31. ESMA agrees that the role of the Monitoring Board should differ for the nomination of the IASB Chair. We support the suggested way forward of approving a set of criteria reflecting the leading characteristics sought in a chair by the Monitoring Board. In addition the Monitoring Board's role in Chair appointments should include an opportunity for it to communicate to the Trustees its assessment of candidates against those criteria, once the Trustees have determined a short list of leading candidates. In line with our preference to build further on the existing three-tiered governance model we think that a final decisions on Chair appointments should remain with the Trustees.
32. The recent problems in appointing a new chair were however a failure of process and timing. ESMA believes that the Monitoring Board should challenge the Trustees to ensure that they get the process right and are listening as appropriate to stakeholders.
33. We also share the view that the Monitoring Board should not have a direct role in the appointment of the IASB Board members and that such a role could potentially erode public confidence in the standard-setting process if public authorities either directly approved or exercised veto rights in the appointment or removal of IASB Board members. We believe that this remains a prerogative of the Trustees guided by the clear principles in the Constitution and with a role for the IFRS Foundation Monitoring Board in the nomination of the IASB Chair as outlined below.
34. In addition, and although we understand the request for confidentiality by the individuals involved, we believe that the Trustees should enhance their communication about the due process applied to this nomination process.

Question 15

Do you agree with the proposal to consider establishing a permanent secretariat for the Monitoring Board to support its increasing roles in overseeing the governance of the standard-setter? Would you support this proposal even if it would require addition financial contributions from stakeholders? Please provide reasons.

35. According to Article 3(B) of the current Charter of the Monitoring Board, the Chair of the Monitoring Board shall provide the group's secretariat services. We understand that providing such resources can be demanding and difficult for the organisation concerned. We are therefore supportive of the idea of a permanent secretariat for the IFRS Monitoring Board and believe that this could contribute to the stability and effectiveness of the Monitoring Board's work. The report of the Monitoring Board clearly outlines some issues (such as the need for clear separation from the secretariat of the IFRS Foundation to ensure the independence of the standard-setter; additional funding re-

quirements and potential sources; but also more practical issues such as the location of secretariat staff headquarters and regional outreach) that would need to be addressed as soon as possible.

36. ESMA believes that consideration should be given to whether there are potential synergies between the IFRS Foundation Monitoring Board and the Monitoring Group of the International Federation of Accountants (IFAC). Apparently, such synergies may exist so in principle ESMA sees merits in the idea of having a joint secretariat for both bodies. This joint secretariat should probably be composed of only a few people at least in the beginning but could be enlarged dependant on the development of the work of both bodies.

Question 16

Do you agree with the need for regular reviews, and the interval of five years as a benchmark? Should the reviews be aligned with the timing of the IFRS Foundation's mandated Constitution reviews? Please provide reasons for your agreement/disagreement.

37. We agree that the role of the IFRS Foundation Monitoring Board will need to be reconsidered regularly. We see merit in doing this at least every five years together with the IFRS Foundation's mandated Constitution Reviews. In addition, we believe that it would be sign of good governance if the Monitoring Board would perform regular effectiveness reviews.

Question 17

Do you have any other comments?

38. We do not have any further comments.