

JOINT LETTER FROM EUROPEAN INVESTOR ORGANISATIONS

Sir David Tweedie
Chair
International Accounting Standards Board
First Floor
30 Cannon Street
London
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12th December 2008

Dear David,

We are writing in advance of the Board's meeting from December 15th-19th which will consider the issues related to IAS 39, and in particular the letter from the European Commission making three further requests with regard to that standard.

We are keen that the voices of users are heard in this debate. The IASB and the IASC Foundation both agree that International Financial Reporting Standards should be designed around the needs of providers of capital to reporting entities. However, the voices of politicians and regulators – and often also the voices of certain preparers with particular individual agendas – have been heard more loudly than those of users. We understand from users who participated in the EU's meeting on October 21st that they do not feel that the Commission's letter reflects their views, as clearly stated to the meeting.

In this context, we would note that our investment institutions have a duty to maximise the savings of millions of individuals who rely on those investments in large part for their financial well-being in retirement. Among these individuals are some 500 million citizens of European Union countries. We and they have an interest in the proper functioning of the financial markets, and that will depend on investors having confidence in the performance reported by public companies.

Due process

Crucial to the maintenance of that confidence, is that the IASB sets standards according to due process so that the information that companies provide is relevant and useful to investors. We accept that the Board's decision to suspend due process in October and to amend IAS 39 may have been appropriate in order to remove the market distortions arising from the discrepancy between US GAAP and IFRS. We do not believe it is a precedent that should be followed, except in the most extreme circumstances.

We would, therefore, argue strongly against any further steps to set aside due process. The issues raised by the European Commission need to be considered with appropriate stakeholder consultation and review rather than rushed through. Any additional hasty moves risk further unsettling market confidence and therefore harming the financial interests of the millions of individuals who are our underlying clients.

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The European Commission's three specific proposals

Market confidence and the interests of our underlying clients will best be served by standards which ensure that companies disclose accurately their financial performance. Standards that allow this information to be masked will leave uncertainty in the minds of investing institutions which is likely to lead to lower, not higher, valuations of the relevant preparers. It is crucial at this time of uncertainty that we move towards a situation where we can rebuild, not undermine, confidence in the market.

Fair Value Option and Impairment of AFS items

We deal with these two issues together because in essence they are both concerns that fair value accounting produces erroneous reporting in the current market dislocations.

In general, we as users hold that the most useful measurement basis for financial instruments should reflect current values. There is an ongoing debate as to whether fair values based on observable market values, provide the best representation of economic reality for financial instruments in illiquid markets. The guidance given by the IASB expert group on valuing financial assets under these conditions addresses part of this problem. Disclosure is particularly important when “mark to model” has been used. The proposed enhancements to IFRS 7 will help to cover this and should be implemented as soon as possible. We would welcome this debate, but do not believe that any change should be made to existing standards ahead of consultation with all stakeholders.

We fear that an option for preparers to reclassify assets currently held at fair value risks undermining confidence by allowing preparers greater discretion to generate reports that they believe are most favourable to them. Furthermore, we do not believe that this is in the long-term interests of economies because this may discourage those preparers from promptly addressing the devalued assets which they hold.

In a similar way, any move to abandon requirements that assets be reported at their current values risks reducing the confidence of users in the figures which preparers provide to them. Any change to the existing current value model for impairments should only occur after discussion and debate with users as well as preparers and regulators.

Embedded derivatives

This is clearly a highly technical area, related to a limited set of assets. As such this request needs to be considered with care by appropriately skilled individuals. We believe that it is simply too abstruse an issue for it to be addressed by the Commission's December 31st deadline.

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We are thus clear that the issues raised by the European Commission in its letter do not merit setting aside due process to meet an artificial deadline. We would welcome their being addressed, but in a way that allows all relevant considerations to be taken into account. This means that there should be some form of public consultation, to allow the IASB's constituents both across the spectrum (users, preparers, etc) and across the globe to respond with their views, even if the consultation period were to be shorter than usual.

Opening space in the IASB's agenda

We would note that investors have been raising concerns for some years over various shortcomings within IAS 39, and we believe that IASB members and staff are aware of these failings.

We strongly believe that there must be a more robust system for ensuring that the IASB's agenda continuously reflects the needs of users. Given the limited resources of the IASB staff, the board should focus on priority projects such as current financial instrument accounting and throw all its firepower towards finalising the improvement required within these projects.

We intend to engage actively with the IASC Foundation to promote ways in which the agenda of the IASB can more effectively address the needs of users and solve problems in standards, rather than be occupied by issues of limited concern or where standards are functioning satisfactorily.

Yours sincerely

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