Deloitte & Touche
Statsautoriseret Revisionsaktieselskab
H. C. Andersens Boulevard 2
DK-1780 Copenhagen V
Denmark

Telefphone: +45 33 76 33 33
Facsimile: +45 33 76 39 93
www.deloitte.dk

Deloitte
Touche
Tohmatsu

5 February 2002

Sir David Tweedie, Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Sir David,

<u>Exposure Draft of a Proposed Preface to International Financial Reporting Standards</u>

Deloitte Touche Tohmatsu and its Member Firms are pleased to comment on the above Exposure Draft issued by the International Accounting Standards Board. Our views are set out in the appendix to this letter.

If you have any questions concerning our comments, please contact Mr. Stig Enevoldsen, chairman of our Firm's IAS Policy Committee, at +45 33 76 36 91.

Yours faithfully
DELOITTE TOUCHE TOHMATSU

Stig Enevoldsen
Partner

Enclosure

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APPENDIX

DELOITTE TOUCHE TOHMATSU COMMENTS
on

Exposure Draft of a Proposed
PREFACE TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

Responses to the Four Questions Asked by IASB:

Question 1

The Board states in paragraph 9 of the proposed Preface that IFRS are designed to apply to the general purpose financial statements of all profit-oriented entities, as defined. The Board also says that although IFRS are not designed to apply to not-for-profit activities in the private sector, public sector or government, entities with such activities may find them appropriate. It notes that the Public Sector Committee of the International Federation of Accountants (PSC) is preparing accounting standards for governments and other public sector entities, other than government business enterprises, based on IFRS. Is the Board's proposed scope clearly defined and appropriate?

We believe that, for now, the restriction of IFRS to general purpose financial statements of all profit-oriented entities is appropriate. Because we believe that convergence of business accounting standards and public sector accounting standards is an important goal, we believe that a close working relationship with the IFAC PSC is essential.

Please see also our response number 8 below (relating to paragraph 9 of the draft Preface) regarding applicability to financial statements of small and medium-sized entities.

Question 2

The Standards issued by the IASC include paragraphs in bold italic type and paragraphs in plain type. The Board is concerned that some constituents may have interpreted the bold italic paragraphs as having more authority, although IASC commentary has suggested otherwise. Paragraph 14 of this proposed Preface states that paragraphs in bold italic type and plain type have equal authority and sets out the Board's intention to discontinue the use of different type styles. The Board intends to provide, in IFRS, robust and useful guidance to illustrate the basic principles in each Standard, including a detailed Basis for Conclusions. Do you agree with these proposals? Why or why not?

We believe that all paragraphs that constitute the "standards" section of an IFRS must be of equal authority, whether they spell out a basic principle, elaborate on a principle, or provide interpretive guidance concerning a principle. The user of IFRS should be absolutely clear as to what is required, and what isn't, under IAS 1.11. Consistent with the IASB's objective of reporting like transactions and events in a like way, as set out in paragraph 13 of the proposed Preface, IFRS should not contain any optional guidance or guidance of uncertain authority. If what is required is clear to the user of IFRS, we favour differentiating the basic principles from the supporting elaboration and interpretation, perhaps by use of a different typeface – in the same way as section headings and subheadings are often useful. Therefore we favour retaining the use of bold italic type for principles and plain type for the elaborative and guidance material. We think this makes the standard more user–friendly and adds clarity. Standards without this distinction can be difficult to follow.

We support the Board's intention to provide "robust and useful guidance to illustrate the basic principles". We are concerned that, in an international environment, there can be a tendency in some jurisdictions to regard guidance as "optional". To ensure credibility of IAS/IFRS financial reports, IASB should do all it can to discourage that view.

Where the robust and useful guidance relates to a particular basic principle, we believe that the guidance should follow the principle immediately rather than be put in an appendix. This view is consistent with our support for continued use of bold italic type for principles. We think this makes the standard more user friendly.

Regarding the basis for conclusions, we note that in the United States the FASB has sometimes, de facto, included standards in its bases for conclusions – standards that the FASB staff has subsequently incorporated in the FASB current text volumes. We believe that IASB should take care to ensure that its bases for conclusions are descriptive of its reasoning but not prescriptive of new guidance. The description should include the principal alternatives considered in developing the standard and the arguments that the Board found persuasive in accepting certain alternatives and in rejecting others.

Question 3

In paragraphs 19 and 20 of this proposed Preface, the Board sets out the due process normally expected to be followed in issuing Standards and Interpretations. Are the Board's proposals appropriate? Are any proposed steps unnecessary? Are there additional steps that should be incorporated?

Please see our responses numbered 14 through 17 below.

Regarding additional steps, we believe that the Preface should clarify the procedures for issuing a draft Interpretation. Paragraph 20(e) of the Preface as exposed for public comment on 8 November 2001 makes no mention of whether or how IASB will be involved with draft Interpretations before they are published by IFRIC for public comment. It is our understanding that at the meeting of the IASC Foundation Board of Trustees on 15 October 2001 the IASB Chairman proposed to the Trustees that:

a. Two IASB members will attend all IFRIC meetings and report back to the IASB.

b. If, based on those reports, five or more members of IASB do not agree with the tentative conclusions reached by IFRIC, the IASB's views would be communicated back to IFRIC before a draft Interpretation is published.

We understand, also, that for the SIC Draft Interpretations published after IASB began operations, IASB has expressed views to SIC and has followed an internal "negative clearance" process (cleared if no more than four IASB members object).

We believe that the Preface should address this important aspect of the development of an Interpretation, particularly in light of recent circumstances in which IASB and SIC disagreed on a number of proposed consensuses. Moreover, the Preface should clarify what procedure will be followed prior to publication of a draft Interpretation if IFRIC is not persuaded to modify its preliminary consensus based on views communicated to IFRIC by IASB. We do not think that IASB or its constituents will be well served if IFRIC publishes draft Interpretations that do not have the support of at least a majority of the IASB members, since final Interpretations require approval of a majority of the IASB.

Question 4

Are there any other matters that should be addressed in the Preface to IFRS?

Please see our responses numbered 19 through 28 below.

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Comments on Specific Paragraphs of the Proposed Preface

1. **Paragraph 1** refers to "the Trustees" and later paragraphs (including 4 and 5) make similar references. When the new IASB constitution was drafted, the legal form of the organisation was not known, and so it could not be more specific than "the Trustees". But the term begs the question "Trustees of what?" A charitable foundation has now been formed known as the IASC Foundation. The second sentence of this paragraph should refer to the Trustees of the IASC Foundation (or, even more precisely, the Trustees of the International Accounting Standards Committee Foundation).

2. **Paragraph 6(a)** states that an objective of the IASB is "to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards...." We think that having two series of standards – IAS and IFRS – might suggest that IASB has two sets of standards, not a "single set". While we recognise the "fresh start" benefits of a new name and new numbering sequence, we think that the global recognition of "International Accounting Standards" and "IAS" is a valuable IASB asset. Moreover, IAS references in local GAAP and local accounting legislation will have to be changed as the name change comes into effect. In our judgement, the change of name from IAS to IFRS is a significant enough matter to warrant a specific request for comments by IASB. We have provided our views separately to the IASCF Trustees in our letter of comments on their proposed changes to the IASC Constitution.

   If the new name is to be IFRS, in keeping with the "single set" mandate we suggest that IASB consider simply renaming the old IASC standards as IFRS and continue the numerical sequence.

3. **Paragraph 6(b)** notes that an objective of IASB is "to promote the ... rigorous application" of its standards. This matter is not addressed in the Preface. We think IASB should explain, in the Preface, its concept of rigorous application.

4. **Paragraph 6(c)** notes that an objective of IASB is "to work actively with national standard-setters to bring about convergence of national accounting standards and IFRS to high quality solutions". This is not exactly what the IASC Constitution states as the IASB objective in this matter. Under the Constitution, the objective is "to bring about convergence of national accounting standards and International Accounting Standards to high quality solutions. Working with national standard-setters is not the objective but a means to the objective. We think the Constitution got it right and the Preface should be modified accordingly. IASB's objectives as set out in paragraphs 6(a) and 6(b) of the proposed Preface are word-for-word from the Constitution, and paragraph 6(c) should be as well.

5. **In paragraph 7**, IASB states that its mission includes establishing standards for "information provided outside financial statements that assists in the interpretation of a complete set of financial statements or improves users' ability to make efficient economic decisions". We commend and support IASB for including this information within its mandate.

6. **In paragraph 7**, the notion of "maximise the convergence of IFRS and national standards" is introduced. We think the word "maximise" is inappropriate because it suggests "convergence at all costs" rather than "convergence of national accounting standards and IFRS to high quality solutions" as stated in IASB's Constitution and in paragraph 6 of the draft Preface. Convergence

is not the objective. High quality solutions to financial reporting questions are the objective. Reword the last sentence of paragraph 7 accordingly.

7. **Paragraph 8** mentions the Framework for the Preparation and Presentation of Financial Statements. Clarify how the Preface relates to the Framework:
   a. This is the Preface to IFRS. Is it also the Preface to the Framework. We note that the Framework has its own Preface.
   b. Elaborate on the authority of the Framework. The Framework is mentioned in paragraph 8, but its status is not explained.

8. **Paragraph 8** notes that IFRS set out presentation requirements. IASB should expressly acknowledge here that presentation is not limited to printed financial statements and printed reports but also includes accounting information presented in electronic media (such as Internet web sites). Otherwise, the term “presentation” will be interpreted too narrowly.

9. While **paragraph 9** says that IFRS apply to “all profit-oriented entities”, we believe that the Preface should address in broad principle the IASB’s approach to considering the special reporting needs of small and medium-sized profit-oriented entities. Further, we believe the third sentence of this paragraph suggests that IASB standards would apply only to some but not all mutual insurance companies and other mutual cooperative entities. Also we believe it should refer to “mutual or cooperative entities” rather than “mutual cooperative entities”. Therefore, we would reword that sentence less restrictively, as follows: “They include organisations such as mutual insurance companies and other mutual or cooperative entities.”

10. **In paragraph 11**, the Preface defines the specific statements included in a complete set of financial statements, including “a statement showing either all changes in equity or changes in equity other than those arising from capital transactions with owners and distributions to owners”. The next two sentences in the same paragraph address interim financial statements but rather than itemise the required interim statements those sentences refer back to IAS 34. We think that cross-referral, rather than itemisation, is the right way to go in the Preface. Accordingly paragraph 11 should not itemise the components of a “complete set” but, rather, the first sentence should refer back to IAS 1. As it is now, paragraph 11, in effect, sets a presentation standard. The Preface should stand the test of time and not need to be revised each time standards are issued. IASB’s performance reporting project may well revise the nature of the statement showing changes in equity, in which case IAS 1 will be revised, but not the Preface.

11. **Paragraph 13.** If it will be IASB policy not to set IFRS that allow alternatives, IASB should say so here. On the other hand, if IASB intends to allow alternatives in IFRS, this paragraph is disingenuous. Paragraph 13 as drafted says that IASB wants like transactions and events to be accounted for and reported in a like way, but paragraph 13 addresses how the Board is going to achieve that objective only with respect to the old IAS. It is silent regarding IFRS. Based on certain tentative decisions that the Board has already made regarding first time application of IFRS and amendments to IAS 39, it appears that IASB will, like its predecessor, find reason to allow options from time to time. If that is the case, we think paragraph 13 might better state that IASB will try to avoid options but that options may sometimes be necessary in the interest of making progress. (An alternative would be not to state, in the Preface, an objective of removing

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alternatives.) To illustrate, paragraphs B47-48 of IAS 40 explain why and how IASC reached a decision to allow two models with respect to measurement of investment property ("will allow preparers and users to gain greater experience working with a fair value model and will allow time for certain property markets to achieve greater maturity").

12. **In paragraph 15,** Interpretations are described as Interpretations of IFRS. The changes to the IASC Foundation Constitution recently proposed by the Foundation Trustees would authorise IFRIC to issue Interpretations that address relatively narrow issues that are simply not addressed in any existing IAS/IFRS. This matter should be clarified in the Preface.

13. We would reword **paragraph 16** so that the introductory sentence does not refer to IAS 1 by name to avoid the need to revise the Preface if the name of the Standard changes. It could say "Under International Accounting Standards, an enterprise whose..."

14. **Paragraph 19(c)** does not accurately describe the Constitutionally-required involvement of the Standards Advisory Council in the due process leading to an IFRS. Paragraph 19(c) of the draft Preface states that the Board will consult with SAC only about the advisability of adding a project to its agenda. Paragraph 36(d) of the Constitution gives SAC a larger responsibility. The Constitution requires the Board to "consult the Standards Advisory Council on major projects, agenda decisions and work priorities". Consulting on major projects means, we believe, soliciting the views of the individuals and organisations represented on SAC on key technical issues in major standard setting projects, not just on agenda decisions. A principal objective in creating the SAC was to give non-liaison standard-setters, more direct input to the IASB. That consultation should involve more than just views on possible IASB agenda projects.

15. **At the end of paragraph 19(e)**, we suggest the addition of the following clause: "normally for an exposure period of not less than 90 days". In an international environment, translation and solicitation of input at the national level by national accountancy bodies are required. A comment period of at least 90 days for discussion documents on major projects is essential. Potential respondents should be aware, for their planning purposes, of what the normal exposure period is expected to be.

16. **At the end of paragraph 19(f)**, we suggest the addition of the following clause: "normally for an exposure period of not less than 90 days". In an international environment, translation and solicitation of input at the national level by national accountancy bodies are required. A comment period of at least 90 days for exposure drafts on major projects is essential. Potential respondents should be aware, for their planning purposes, of what the normal exposure period is expected to be. Paragraph 19(f) should also acknowledge that for exposure drafts on relatively small issues the Board may conclude that a shorter period is appropriate.

17. **At the end of paragraph 20(c)**, we suggest the addition of the following clause: "normally for an exposure period of not less than 60 days". In an international environment, translation and solicitation of input at the national level by national accountancy bodies are required. A comment period of at least 60 days for draft Interpretations is essential. Potential respondents should be aware, for their planning purposes, of what the normal exposure period is expected to be.

Deloitte Touche Tohmatsu

18. The second sentence of **paragraph 23** should begin "Until the effective date of a new or amended IFRS" rather than "Until an IFRS is completed".

Other Matters that Should Be, But Are Not, Addressed in the Proposed Preface

19. **IASB precepts.** The mission statement of the US Financial Accounting Standards Board includes the following statement of precepts. We suggest that IASB consider including similar precepts in its Preface:

> The Board follows certain precepts in the conduct of its activities. They are:
>
> - *To be objective in its decision making* and to ensure, insofar as possible, the neutrality of information resulting from its standards. To be neutral, information must report economic activity as faithfully as possible without coloring the image it communicates for the purpose of influencing behavior in any particular direction.
> - *To weigh carefully the views of its constituents* in developing concepts and standards. The ultimate determinant of concepts and standards, however, must be the Board's judgment, based on research, public input, and careful deliberation, about the usefulness of the resulting information.
> - *To promulgate standards only when the expected benefits exceed the perceived costs.* While reliable quantitative cost-benefit calculations are seldom possible, the Board strives to determine that a proposed standard will fill a significant need and that the costs it imposes, compared with possible alternatives, are justified in relation to the overall benefits.
> - *To bring about needed changes in ways that minimize disruption to the continuity of reporting practice.* Reasonable effective dates and transition provisions are established when new standards are introduced. The Board considers it desirable that change be evolutionary to the extent that can be accommodated by the need for relevance, reliability, comparability, and consistency.
> - *To review the effects of past decisions* and interpret, amend, or replace standards in a timely fashion when such action is indicated

20. **IASB agenda selection.** While the Preface spells out the due process for a project once it has been placed on IASB's agenda, the Preface is silent as to how agenda projects are identified and how they are formally added to IASB's agenda. We believe this should be addressed in the Preface, including whether public input will be solicited.

21. **IFRIC agenda selection.** While the Preface spells out the due process to be followed by IFRIC and IASB once a project has been placed on IFRIC's agenda, we believe the Preface should indicate how agenda projects for IFRIC will be selected, including (a) whether public input will be solicited and (b) the role and composition of IFRIC's agenda committee.

22. **Availability of comment documents on the Internet at no charge.** In paragraph 19 or elsewhere, IASB should state that all comment documents – discussion documents, exposure

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drafts, and proposed Interpretations – will be made available without charge in electronic form on the IASB website. We believe that the public interest requires that constituents be given free access to proposals that will affect them, so that they can comment.

23. **IASB public record.** We believe that the Preface should be clear about IASB's public record for agenda projects:

    a. What is and what is not included in the public record to which constituents can have access (staff drafts, drafts provided to the Board for Board meetings, letters of comment received on discussion documents and exposure drafts, correspondence).

    b. How the public can access documents that are included in the public record (IASB web site? Public reference room at the IASB offices? Obtain printed copies by paying a fee?)

24. **Re-exposure.** We believe that the Preface should describe IASB's general policy toward when re-exposure of an exposure draft or proposed Interpretation is appropriate.

25. **Staff guidance.** The Preface should address the issue of staff guidance, including how that will (or will not) be provided in written form, electronic form, and telephonic form. We include within "staff guidance" both responses to individual technical enquiries and staff guidance publications of the sort that have been issued by FASB staff.

26. **Language.** The Preface should state IASB's objective of using "plain English" in all IASB documents. As IASB Standards are being applied on a global basis and in a large number of countries where English is not the first language, such an objective would help make IASB documents accessible to a broader community.

27. **Public availability of all Board and IFRIC meeting papers.** All agenda papers that are discussed at an open meeting of the IASB or its Interpretations committee should be made public in advance of the meeting. Our firm has had one or more observers at every IASB meeting since inception, and they often find it difficult or completely impossible to follow the discussion because of constant reference to paragraphs in the Board papers. Observer notes just are not enough. Observers should have access to the same papers that are in front of the Board members – with appropriate cautionary language on them that accurately describes their status. If the Board believes that providing all papers that are in front of the Board members at a public meeting is onerous, then at a minimum all key papers that are necessary for an understanding of the debate should be publicly available in advance of the meeting. An open due process should really mean fully open. We would note that making these papers available will actually reduce the workload on the Board's technical staff because there would not be a need to draft, review, and publish separate observer notes.

28. **Lead time for new Standards.** We believe that the Preface should expressly state an IASB policy regarding the lead time for new Standards – the time between publication and effective date. We believe that the Board should say that this will not normally be less than one year. Moreover, the year period should be measured from the date that the full text of the Standard is publicly available, not when it is voted on. In an international environment, translation, dissemination, education, and modification of local GAAP take a long time. In many

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jurisdictions, IAS/IFRS will be vastly different from existing accounting and disclosure practices, requiring considerable study and systems redesign. A year is not an unreasonable minimum transition period.