

The Trustees of the International Accounting Standards
Committee Foundation
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31 March 2009

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Dear Sirs

Invitation to comment: Review of the Constitution - Identifying Issues for Part 2 of the Review

The global organisation of Ernst & Young is pleased to submit our response to the questions raised in the above discussion document.

We would like to draw your attention to a number of key points, which we have summarised in this letter. These relate to the 'fast track' procedure, the International Accounting Standards Committee Foundation's (IASCF) funding process, the reconstituted Standards Advisory Council (SAC) and the role of the Monitoring Board in the International Accounting Standards Board's (Board) agenda setting process. Our detailed responses to specific questions in the discussion document are set out in the Appendix to this letter.

Fast track procedure

We believe that a fast track procedure should be created. However, to ensure that it is sufficiently robust, the fast track procedure must:

- (1) Define a set of principles to help the Board determine which situations constitute 'great urgency'. These principles should set a very high hurdle for an issue to qualify for the fast track procedure.
- (2) Establish an appropriate timeframe for constituents to provide comments (at least two weeks). The process must also allow due time for the Board to consider these responses.
- (3) Prohibit backdating the effective date of amendments.

In our view, the IASCF should provide comprehensive proposals for a fast track procedure for public comment as a matter of high priority.

To supplement the fast track procedure, we believe that the International Financial Reporting Interpretations Committee (IFRIC) should work more closely with regulators in dealing with difficult and urgent interpretation issues, at an early stage, to avoid divergence in practice. This could be either done directly or through the Monitoring Board.

Funding process

Part of the Monitoring Board's role is to monitor the IASCF's funding process. Providing a sufficiently independent funding mechanism is a key requirement for a number of jurisdictions planning to adopt IFRS. We are encouraged that the Trustees have succeeded in establishing national funding regimes, consistent with their own funding principles, in a number of countries. To supplement this, we believe that the Trustees must demonstrate to the Monitoring Board that they have established a clear funding roadmap, which includes jurisdictions moving to IFRS. This will further increase the Board's transparency and independence. The Trustees should also obtain the Monitoring Board's approval of the IASCF's overall funding process as this will enhance the connection between the IASCF and regulators and, in turn, the broader overall acceptance of IFRS by regulators.

Reconstituted SAC

We are pleased with the recent changes to the SAC's constitution and operating procedures. Specifically, we support the requirement for the Board to explain why they have not included an issue on their agenda that has been recommended by the SAC in a formal vote. We suggest that the Trustees be charged with ensuring that the Board duly considers the recommendations of the SAC to ensure that this process works effectively. The Monitoring Board should ensure that the Trustees carry out this duty as part of their broader oversight role.

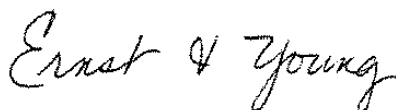
Role of the Monitoring Board

We believe that the ongoing independence of the Board is absolutely fundamental. Consequently, it is imperative that the forthcoming amendments to the Constitution, and the way they are put into practice, ensure that the Monitoring Board does not have undue influence over the Board's agenda setting process.

The Trustees and Monitoring Board need to demonstrate that the standard-setting process is sufficiently independent and robust so that regulators accept IFRS, as issued by the Board, without the need for a further endorsement process. We describe how we believe that this can be achieved in our response to question 9 in the Appendix to this letter.

We would be pleased to discuss our comments further with the IASCF, at your convenience. Please contact Will Rainey at 020 7951 3619.

Yours faithfully

A handwritten signature in cursive script that reads 'Ernst & Young'.

APPENDIX

Objectives of the organisation

1. *The Constitution defines the organisation's primary objective in the following manner:*

to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions

In fulfilling that objective, the organisation is

to take account of, as appropriate, the special needs of small and medium-sized entities and emerging economies

Does the emphasis on helping 'participants in the world's capital markets and other users make economic decisions', with consideration of 'the special needs of small and medium-sized entities and emerging economies', remain appropriate?

We believe that the emphasis in the objective remains appropriate, with the exception of the needs of 'emerging economies'. In our view, this term should be removed as there is no need to continue to specifically consider these economies. All countries converting to or currently reporting under IFRS will use or currently use full IFRS. Alternatively, they will adopt IFRS for Non-publicly Accountable Entities, regardless of whether they are emerging economies or not.

2. *In the opinion of the Trustees, the commitment to drafting standards based upon clear principles remains vitally important and should be enshrined in the Constitution. Should the Constitution make specific reference to the emphasis on a principle-based approach?*

We believe reference to the emphasis on a principle-based approach to standard setting should be included in the Constitution. It should be the Board's primary basis for standard setting. However, some standards and interpretations will continue to require application guidance. Therefore, any amendment should not preclude the use of application guidance.

We also believe that the term 'principle-based' should be defined to ensure that standards and amendments are developed on a consistent basis.

3. The Constitution and the IASB's Framework place priority on developing financial reporting standards for listed companies. During the previous review of the Constitution some commentators recommended that the IASB should develop financial reporting standards for not-for-profit entities and the public sector. The Trustees and the IASB have limited their focus primarily to financial reporting by private sector companies, partly because of the need to set clear priorities in the early years of the organisation. The Trustees would appreciate views on this point and indeed whether the IASB should extend its remit beyond the current focus of the organisation.

We do not believe that the Board should extend its focus to not-for-profit entities and the public sector at this time. The Board's current work programme is extensive. Broadening its remit would delay current projects, which would be an undesirable consequence. In addition, the Board is already involved in the project work of the International Public Sector Accounting Standards Board (IPSASB), which focuses on the accounting and financial reporting needs of the public sector. Therefore, there is no immediate need for the Board to focus on the specific needs of accounting for the public sector.

4. There are other organisations that establish standards that are either based upon or have a close relationship with IFRSs. The IASC Foundation already recognises the need to have close collaboration with accounting standard-setting bodies. Should the Constitution be amended to allow for the possibility of closer collaboration with a wider range of organisations, whose objectives are compatible with the IASC Foundation's objectives? If so, should there be any defined limitations?

We believe that this question is ambiguous. The Board currently consults with other organisations appropriately and the Constitution does not need to be amended for this activity to continue. However, it is important that any interaction with other organisations does not undermine the independence of the Board's agenda setting process, or indeed International Financial Reporting Standards themselves.

Governance of the organisation

5. The first part of the review of the Constitution proposed the establishment a formal link to a Monitoring Group. Under this arrangement, the governance of the organisation would still primarily rest with the Trustees. Although the first part of the review has not yet been completed, the Trustees would welcome views on whether the language of Section 3 should be modified to reflect more accurately the creation of the Monitoring Group and its proposed role.

Modification of Section 3 is necessary to reflect the creation of the Monitoring Board and to define its role. However, we believe it is imperative that the forthcoming amendments to the Constitution clearly prohibit the Monitoring Board from having undue influence on the Board's agenda setting process.

Trustees

6. The Trustees are appointed according to a largely fixed geographical distribution. Is such a fixed distribution appropriate, or does the current distribution need review?

In our response to Part 1 of the Review, we disagreed with the proposal that the Board's composition be based on geographical criteria. We continue to believe that the issue of greatest importance is to have members of the highest possible quality. Setting strict geographical criteria will potentially detract from this objective. In our view, the IASCF's constitution should reflect the current language applicable to the composition of the Board – that is, selection is not based on geographical criteria. However, membership should not be dominated by any particular constituency or interest.

7. Sections 13 and 15 set out the responsibilities of the Trustees. The intention of these provisions is to protect the independence of the standard-setting process while ensuring sufficient due process and consultation—the fundamental operating principle of the organisation. In addition to these constitutional provisions, the Trustees have taken steps to enhance their oversight function over the IASB and other IASC Foundation activities. The Trustees would welcome comments on Sections 13 and 15, and more generally on the effectiveness of their oversight activities.

Sections 13 and/or 15 will need to be updated to reflect the responsibilities of the Trustees to the Monitoring Board. We believe that any updates should include a requirement that the Trustees demonstrate to the Monitoring Board that an appropriate funding mechanism has been established or is in the process of being established within a reasonable timeframe. This mechanism must ensure the independence of the IASB. We believe that appropriate monitoring and approval of the funding process is essential to both enhance the independence of funding and bring broader overall acceptance of IFRS by regulators. Refer to our response to question 8 for more detailed views on the funding process.

8. The Trustees are responsible for ensuring the financing of the IASC Foundation and the IASB. Since the completion of the previous review of the Constitution, the Trustees have made progress towards the establishment of a broad-based funding system that helps to ensure the independence and sustainability of the standard-setting process. (For an update on the funding status, see <http://www.iasb.org/About+Us/About+the+IASC+Foundation/Funding.htm>) However, the Trustees have no authority to impose a funding system on users of IFRSs. The Trustees would welcome comments on the progress and the future of the organisation's financing.

We agree with the funding principles set out by the Trustees in the funding system referred to in this question. The Trustees must work directly with the various securities regulators and others responsible for enforcing IFRS, to obtain funding that is not contingent on any action that would hinder independence. Provision of a sufficiently independent funding mechanism is a key requirement for a number of jurisdictions planning to adopt IFRS. We are therefore encouraged that the Trustees have succeeded in establishing national funding regimes, consistent with their own funding principles, in a number of countries.

To supplement this, we believe that the Trustees must demonstrate to the Monitoring Board that they have established a clear funding roadmap, which includes jurisdictions moving to IFRS. This will further increase the Board's transparency and independence. The Trustees should also obtain the Monitoring Board's approval of the IASCF's overall funding process as this will enhance the connection between the IASCF and regulators. We believe that this connection will both enhance the independence of funding and ensure the broader overall acceptance of IFRS in a number of jurisdictions.

International Accounting Standards Board

9. Commentators have raised issues related to the IASB's agenda-setting process. The Constitution gives the IASB 'full discretion in developing and pursuing its technical agenda'. The Trustees have regularly reaffirmed that position as an essential element of preserving the independence of the standard-setting process. However, they would welcome views on the IASB's agenda-setting process and would appreciate it if, in setting out views, respondents would discuss any potential impact on the IASB's independence.

We believe that the ongoing independence of the Board is absolutely fundamental. The Trustees and Monitoring Board need to demonstrate that the standard-setting process is sufficiently independent and robust so that regulators accept IFRS, as issued by the Board, without the need for a further endorsement process. We believe that this regulatory acceptance will be achieved if the Board demonstrates that it:

- (1) Consults with as many different constituents as possible;
- (2) Listens to constituents' views; and
- (3) Is sufficiently flexible in dealing with fast changing circumstances.

The Board must simultaneously continue to take account of due process and disclose how constituents' comments have been addressed. We also believe that independence will be enhanced if the Monitoring Board is satisfied that the Trustees have ensured that the Board complies with due process. However, this can only be achieved if the Monitoring Board has genuine power to provide oversight.

10. The Constitution describes the principles and elements of required due process for the IASB. The IASB's procedures are set out in more detail in the IASB Due Process Handbook. If respondents do not believe the procedures laid out in the Constitution are sufficient, what should be added? If respondents believe that the procedures require too much time, what part of the existing procedures should be shortened or eliminated? The Trustees would also welcome comments on recent enhancements in the IASB's due process (such as post-implementation reviews, feedback statements, and effect analyses) and on the IASB Due Process Handbook.

We agree with the Board's procedures as set out in the *IASB Due Process Handbook*. However, we believe that the feedback statements process can be improved. For example, we felt that the feedback statement for the revised IFRS 3 *Business Combinations* (IFRS 3R) did not adequately address constituents' concerns about the treatment of goodwill.

Therefore, we expect that the Board will pay greater attention to these concerns in the post-implementation review of IFRS 3R. We believe that it is essential that all constitutional requirements, such as feedback statements, be carried out thoroughly to ensure the credibility of the standard setting process.

11. Should a separate 'fast track' procedure be created for changes in IFRSs in cases of great urgency? What elements should be part of a 'fast track' procedure?

We believe that a fast track procedure should be created. However, to ensure that it is sufficiently robust, the fast track procedure must:

- (1) Define a set of principles to help the Board determine which situations constitute 'great urgency'. These principles should set a very high hurdle for an issue to qualify for the fast track procedure.
- (2) Establish an appropriate timeframe for constituents to provide comments (at least two weeks). The process must also allow due time for the Board to consider these responses.
- (3) Prohibit backdating the effective date of amendments.

In our view, the IASCF should provide comprehensive proposals for a fast track procedure for public comment as a matter of high priority.

To supplement the fast track procedure, we believe that the International Financial Reporting Interpretations Committee (IFRIC) should work more closely with regulators in dealing with difficult and urgent interpretation issues, at an early stage, to avoid divergence in practice. This could be either done directly or through the Monitoring Board.

Standards Advisory Council

12. Are the current procedures and composition, in terms of numbers and professional backgrounds, of the Standards Advisory Council (SAC) satisfactory? Is the SAC able to accomplish its objectives as defined in Section 38?

The criteria for the composition of the SAC are appropriate and should continue to be applied to achieve an appropriately balanced range of members, from relevant parties, who have an interest in financial reporting. SAC members should continue to include preparers, auditors, users and regulators with diverse geographical backgrounds. Consistent with our views expressed in question 6, we believe that the issue of greatest importance is to have the highest quality members possible and are pleased that no strict geographical criteria for membership of the SAC have been proposed.

However, we observe that the SAC could provide more timely input to the Board if their meetings were held more frequently and on an ad-hoc basis, or through sub-groups, as required.

We are also pleased with the recent changes to the constitution and operating procedures of the SAC. Specifically, we support the requirement for the Board to explain why they have not included an issue on their agenda that has been recommended through formal vote by the

SAC. We suggest that the Trustees be charged with ensuring that the Board duly considers the recommendations of the SAC to ensure that this process works effectively. The Trustees should specifically ensure that the Board provides an appropriate response if they do not add an issue to their agenda. The Monitoring Board should ensure that the Trustees carry out this duty as part of their broader oversight role.

13 Attached to this discussion document are the terms of reference for the SAC, which describe the procedures in greater detail. Are there elements of the terms of reference that should be changed?

Refer to our response to question 12.

Other issues

14. Should the Trustees consider any other issues as part of this stage of their review of the Constitution?

We have no further comments to make.