IASB Chairman's Opening remarks to the European Parliament

Committee for Economic and Monetary Affairs

Brussels, 1 December 2014

The success of Europe's Capital Markets Union project largely depends on its ability to attract capital from around the world, and a vital ingredient to achieving this goal is internationally accepted financial reporting standards.

Building a credible Capital Markets Union

Opening remarks by Hans Hoogervorst, Chairman,
International Accounting Standards Board

*****

I am grateful for this opportunity to speak with your committee on IFRS and the IASB. I truly believe that high quality accounting has never been more important to Europe than is currently the case. The financial crisis has made Europe realise it must reduce its dependence on bank finance. For this reason, the European Union wants to create a Capital Market Union. Through this Capital Market Union, companies must be given better access to the capital markets.

The capital markets can indeed help in providing more oxygen to credit-starved European businesses. But for capital markets to function well, they need to be properly regulated. Capital markets are rife with short termism and conflicts of interests. Wherever people work with other people's money, regulation is necessary to prevent abuse and moral hazard.

Accounting standards are an essential part of the regulatory infrastructure of capital markets. Reliable financial information is indispensable for trust and confidence in our market economy. The IASB seeks to bring accountability and transparency to the capital markets. The public interest of our job is to help keep markets honest.

In the past, the IASB has fought tough battles to expose hidden costs and liabilities to the sunlight of transparency. Investors now know the full costs of stock options and pension liabilities. Hopefully they will soon have full clarity on the hidden debt behind leases. In all of these cases, vested interests have protested vigorously. The discipline we impose on private markets is rigorous. Much more rigorous, sadly, than the discipline of public sector accounting in many countries around the world.

As you know, the Commission is currently evaluating the impact of IFRS in the EU. We do not expect this evaluation to say that IFRS is perfect, because we know it is not. Still, we feel pretty confident that the verdict will be that, overall, IFRS has had a positive impact on the European economy. Let me explain the grounds of my optimism.

First, IFRS provided the European market in 2005 with a single accounting language. Before the adoption of IFRS, the EU had a myriad of accounting languages. European pension funds and other institutional investors and creditors just had to go and figure it out.

The introduction of IFRS was a game changer in terms of investor protection. IFRS created much needed transparency and comparability to investors in Europe. The national securities regulators, now joined in ESMA, could finally start to compare notes and improve enforcement.

The gain for investors was also a gain for companies. They now have a level playing field in accounting. The ability to work with one accounting language throughout Europe is also a big cost saving for companies.

Since the EU set the example of adopting IFRS, most of the rest of the world followed suit.

114 countries have fully adopted IFRS, while 12 more permit its use. All of Europe, all of Latin America, Canada, and most Asian countries use IFRS.

The use of IFRS is spreading fast among Chinese and Japanese companies. The United States is still holding out, but even there European companies can use IFRS for their listings on the American stock markets.

The spread of IFRS around the world is an enormous benefit for European investors such as pension funds. They need to invest in dynamic emerging markets to generate good returns for their pensioners. Thanks to IFRS they now can understand the financial reporting of Korean, Brazilian and many African companies. For European businesses, IFRS has led to a reduction of costs. It has lowered the cost of capital and has reduced the accounting costs of their foreign subsidiaries.

A large majority of the 114 countries that have adopted IFRS have done so without making any local adaptations. The fact that they have resisted tinkering with IFRS does not mean that they agree with everything we do. But everyone realises that if every country starts making its own adaptations, the benefits of a single set of global standards will simply vanish into thin air.

Except for one, limited, carve-out, Europe has also adopted all of our Standards. This does not mean that the EU has relinquished its sovereignty on accounting standards. Europe does not accept our Standards blindly. Indeed, of all jurisdictions, Europe has by far the most elaborate endorsement procedure, which includes EFRAG, the Commission, the European Council and your Parliament.

The IASB knows that if we do not take Europe's input in our standard-setting seriously, we put endorsement at risk. So you can rest assured that the IASB does not take Europe for granted, quite the opposite. At the same time, we hope Europe understands that as a global organisation we cannot be seen to be listening to Europe alone. Obviously, we have to listen to our non-European constituents as well.

I am sure the EU-evaluation of IFRS will also contain critical remarks. We try to improve where we think criticism is fair. We acknowledge financial statements may have become too long. We are reviewing our disclosure requirements to reduce the overload of boilerplate disclosures. We understand the concerns of investors who fear unwarranted profit taking on the basis of flimsy valuations. In our new *Conceptual Framework for Financial Reporting*, we will make clear that prudence should be exercised to prevent overstatement of assets and profits. We are also against understatement of liabilities, which is why lease commitments need to brought to the balance sheet.

While we listen carefully to criticism, we need our independence to avoid capture by special interests, just like central bankers need their independence from the financial industry and politics. Regulatory capture was an important cause of the financial crisis. So we need to keep special interests at bay. We will listen to everyone, but always have the public interest at heart.

Let me draw to a conclusion. We very much welcome Europe's ambition to create a European Capital Market Union. The existence and use of a set of high quality accounting standards such as IFRS is absolutely crucial to making this ambition come true. Capital markets can only function well with proper regulation. IFRS Standards are an essential part of this regulation. The IASB stands ready to give Europe the tools it needs to fulfil this important ambition.