# IASCF Trustees and Monitoring Board Meeting, 15.45 – 17.30
# 1 April 2009

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## Speaker key

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| AV | Antonio Vegezzi |
| CB | Clements Börsig |
| CM | Charlie McCreevy |
| DT | Sir David Tweedie |
| DS | David Sidwell |
| GL | Guillermo Larrain |
| GT | Greg Tanzer |
| GZ | Chairman – Gerrit Zalm |
| HH | Hans Hoogervorst |
| JE | Julie Erhardt |
| JM | Junichi Maruyama |
| JvR | Jeff van Rooyen |
| LS | Luigi Spaventa |
| MS | Mary Schapiro |
| OF | Oscan Fanjul |
| PM | Pedro Malan |
| PT | Paul Tellier |
| RG | Robert Glauber |
| SD | Sam DiPiazza |
| SM | Sylvie Matherat |
| TS | Tom Seidenstein |
| UM | Unidentified man |

GZ Okay, welcome back again, and a special welcome for Guillermo who came in late, but we knew that. And he'll give us an update on emerging markets and IFS adoption. Guillermo, the floor is yours.

GL Thank you very much, Chairman. As you know, the situation in emerging markets has been getting worse over the last couple of quarters, and at the emerging markets committee at IOSCO, we ran a survey, two surveys; the first one to understand a little bit which were the sources of instability and turmoil in different emerging market jurisdictions, and a second one on what was going on with the adoption of IFRS and fair value. The first survey was sent to jurisdictions in January, so we have now quite a lot of answers from them. The second survey was sent after the Washington meeting in February, so we have received a smaller amount of answers and, therefore, what we can say about the adoption of IFRS up to now, it's relatively not very certain. So let me say first that what our regulators are telling us in that survey is that most jurisdictions in emerging markets were not really exposed to subprime instruments at the source of the crisis. So when everything started to fall down, to fall apart, the emerging markets were not really exposed to that. What has happened is that they have been affected in the second round much more by financial and macroeconomic considerations rather than by valuation issues. So the huge cut in terms of trade, depressed demand for exports in several jurisdictions, the increase in interest rates for financing the operation of the local economies, in some cases, the difficulty in having access to international financial markets, that is the real domain problem that emerging economies are facing now. And it is in that context that valuation problems have arisen and, of course, have had impact in emerging market economies. The survey that, as I said, was answered was answered by something liked 38 countries, so it's not very large, the sample. In particular, we don't have the largest jurisdictions answering the survey. What we can say preliminarily is that almost all jurisdictions that have responded are applying for a value to financial... to value financial instruments, that is really clear. And approximately half of the countries that have reported have introduced changes in their accounting standards to value financial instruments that companies must present before securities regulator. And this is linked, as they say, to face the turmoil in the last part of 2008. So what we can inform you is that a significant amount of jurisdictions have moved away to some extent to fair value accounting as a response to the crisis, because this was creating trouble in different financial sectors. That's what I can really tell from now on. We plan to make this questionnaire again, and eventually... well, the two questionnaires will be sent again to our members in order to have a more, a better information to share with you eventually in the next meeting. I presume that it was for July. Unfortunately, I cannot tell much about this, but that's what I can report.

GZ Thank you for your concise report. Are there questions or remarks? I'm also looking at the Trustees from emerging countries. Pedro?

PM Well, very briefly, just to let you know, most of you are informed that it's the law of the land. In Brazil, it was approved in December 2007 after seven years in Congress. It went to three committees. We are going to adopt... not adapt, to adopt IFRS, and we make... And I think it's very important for a discussion about adoption in some of the emerging markets, the distinction between adoption and adaptation. Adaptation I think is something should be avoided. I understand the meaning of the word convergence, that people think to converge to IFRS, but the law that we approved in December 2007 in Brazil already incorporated a lot of features of adopted. It incorporated adoption of IFRS which since was sanctioned by the President immediately after, they are effective from 1st January 2008 already. And the IFRS will be the law of the land in Brazil in 2009 for most companies, and 2010 at the latest. And I do hope in... I do believe in demonstration effect in externalities, and network externalities. I'm sure that the Brazilian adoption, given the weight and the gravitas of the country in the region, will have an effect in stimulating other countries in not only Latin America, but in other parts of the emerging world to move ahead. We attach an enormous importance, and I listen with great interest Mr. Hoogervorst, Mr. McCreevy, Mr. Maruyama and Ms. Schapiro and Ms. Matherat today saying that they also are committed to the convergence, to the adoption of a single set of global transparent set of standards for financial reporting, and this is music to the ears of many of us here. I understand very much the concern about, say, the accountability and the transparency and the counterparts of an independent standards setting body, but I think we should use the present crisis, we mentioned this in our internal discussion just with Trustees in the morning in our closed session, the idea that the crisis that we are going through, although posing a lot of problems, it also should not be a missed opportunity for us to speed up the process of convergence. I refer especially to the IASB and

FASB, IFRS and the US GAAP in a reasonable timeframe, I'm looking for 2011 as a good decision point for the US on the basis of the progress that we are going to achieve as I hope from now to then. And I hope a decision there could be taken on the basis of such progress to move forward. And as we do so, I think that other emerging markets would gradually, as some of them have announced already their intention to do so, converge towards IFRS. So I did not want to intervene in the previous discussion, but most of us who endorse the joining of the Monitoring Board to our... to the working together with the Trustees, saw this as an example say we have moved, and it was a major achievement what we have done so far. And I think Mr. McCreevy is right. Europe has played an important role to that in 2002 and decision about 2005 adoption. And bringing together the regulators, the US, the Japanese and the European regulators IOSCO to this forum, for me and for many of us was an expression I'd say, well, that's the time to give an added push, give more momentum to something which is going on. And the crisis, the current crisis, instead of making us to go in a slower motion, and stop to think, it should be an opportunity to try to take a medium term view, not to try to respond on an ad hoc basis to the demands which sometimes occur for quarterly reports of certain sectors and areas, but try to take a broad view on how could we establish a system, a global system of a set of international financial reporting which would help us. How could we avoid a repetition of the very dire straits that we have now? And I'm sure that we could do a lot if we work together. That's why I welcome you, the Monitoring Board, and we are looking forward to work together with you in the next few weeks, months and years, and to have a common objection, to have a single set of transparent, global set of financial standards. And we count on your collaboration, cooperation with us, and we are ready to cooperate with you. And in our case, since this is unclassified, some of us is representing far away, exotic, emerging markets, there will be a large number of far away, exotic, emerging markets joining IFRS as we move forward. I can assure you of that. Thank you.

JvR Chairman, just a couple of observations. As you know, South Africa was amongst the first ten countries to actually adopt IFRS. And we did this for commercial reasons. If you look at South Africa today, we certainly rank in the top 20 if you look at the market capitalisation of the major stock exchanges around the world. So we've certainly benefited from having adopted IFRS. I think something like 40% of investors on our capital markets are foreign investors, and the fact that they can pick up a set of financial statements in South Africa and compare it to a set of financial statements anywhere in Europe is certainly beneficial. We've actually gone beyond just the full adoption of IFRS. We've also been piloting the SME standard, now also referred to as the private entities standard. And that's also working very well for us in South Africa. And I just wanted to ask a general question around emerging markets, because last week, for example, I was in Ghana, and I had an opportunity to speak to the central bankers in Ghana. And they were also saying to me that they want to... that within the next couple of months, it will become mandatory for the banks in Ghana to use full IFRS. And the question that I asked them was, so their hearts are certainly in the right place, but what capacity have you got in Ghana? Because really, IFRS, it's fine to say you want to adopt IFRS, but have you actually got the skills base in Ghana to actually do this? So my general question is I think in emerging markets there's certainly a problem around capacity, and I think perhaps in this survey, this questionnaire that you're talking about, it might be worthwhile just exploring whether there's scope for those countries to start off, just to get some exposure to IFRS, start off looking at adopting the SME standard, or the private entities standards, because it's not as complicated as the full IFRS, and often you will find that even local standards don't compare to the SME standards. So that's a very good way of actually getting into this to begin to build the skills base.

DT Just picking up on Jeff's point, and I didn't mention this to the Trustees this morning, but we voted to issue the SME standard which we published in June, the final version. And it's going to be about 250 pages, compared to 2,500 of full IFRS. Our biggest problem now is the name. We've tried SMEs, and people objected to size criteria. We then tried private which means certain things in certain countries. So we asked the national standard setters to come up with a name, and they came up with not publicly accountable entities, but that got translated into nappies, and we know what that contains, so we're now thinking desperately for a name. But otherwise, it's finished. That's what's holding us up at the moment, but it has been very well received.

SD Just to comment on the emerging markets, we have probably $5 billion to $6 billion of our revenue in the emerging markets, and each of the other big networks have as well. And a major part of that is in the insurance side. And I think the progress being made in training, developing the capacity using Jeff's question of the professionals in that space is very, very good. Of our maybe 30,000 auditors in the emerging markets, probably two thirds of them have now gone through formal IFRS training, even in countries that have not yet adopted or that are on the path like India of adoption somewhere down a few years from now. So actually, I think the momentum in the emerging markets around capacity is moving very, very rapidly, and I think the training is putting those markets in good position. The other point I would make, and often criticised or questioned, is whether the flexibility, the principles based, gives too much flexibility in the emerging markets. We haven't found that at all. We've found the emerging markets to be reasonably disciplined about operating in a way that is just as robust as what we've seen in the developed markets. So I think the emerging markets are coming on very well. The SME, or whatever you want to call this thing, has great momentum in many of these markets.

UM I have a question to Guillermo. If I understood him correctly, some of the emerging markets are now moving away a little bit from fair value accounting because of the current circumstances. It's something that a lot of people would like to do here too. But my question is, are things going better now in these countries?

GL I will start with the last. If we were able to isolate the various effects and to say what's the marginal effect of each of them, it would be great, but we are not as fortunate as that, so I cannot really have an idea. But the fact is that several countries are moving in that direction. Now it's very interesting Jeff's points concerning the SMEs. And well, the name is something that is important because it's symbolic. But the point is that, as Sam was saying, the effort that emerging markets are currently doing in capacity building, it's enormous. In Chile, we are moving to, as Brazil, to adopt, not to adapt, to the point that our... no, that's very symbolic as well, to the point that what we recognise as the IFRS is the English version published by the IASB. It's not... even the Spanish translation that you have, not even the translation that our accountants are making in (unclear) is the English one, so just in order to have in the last version of it. But the problem is that I'm not sure, because I haven't seen it, what's the conceptual difference between the SMEs approach? I presume that it's not much, but eventually there may be some differences, and the full fledged IFRS. So to some extent, could it be possible to say now after having done such an enormous effort, can you step one or two notches below, because you will now use the SMEs' approach. I'm not sure. What I want to say is that I believe that we must discuss a strategy for emerging markets, first of all because the whole thing about a common language in this case in this subject is that everyone will speak exactly the same language. Well, I have here country by country the answers, and

I was just looking at some countries say these national standards based on IFRS. I'm not talking about fair value, I'm just talking the general thing. Other countries which are making their own translation which are based in the IFRS; other countries who say that this has developed their own based on this. I mean, we need to really try to converge to exactly the same norm. Now to converge to exactly the same norm, my feeling is that this accountability process that we were discussing in the previous session, it's very important. It's important for... because the standards that will be developed here will be... should be used by everyone. And, therefore, they accountability, it's very important. But on the other hand, we need to take into consideration that emerging market jurisdictions have peculiarities that you don't have in emerging markets. The first one is how liquid those markets are and how reliable those prices are. We have discovered in developed markets the problem of illiquidity, but it's something that we live every day. And, therefore, I'm not sure whether we need to make some further consideration in that respect, and I am not sure because I haven't see it if the SME standard is close to that. My feeling is that we need to make a strategy for emerging markets and to have a monitoring of how that strategy could eventually start to be implemented.

GZ Thank you. Anybody else on emerging markets and IFRS? So if that's not the case, we go to the main dish, and that is the response to the financial crisis. We have some time for that. I think if you connect financial crisis to accounting standards, one thing is in my view certain; that it shows a need for uniform, high quality accounting standards. What is a danger for accounting standards, be it arbitrage, or as an economist I remember Gresham's Law; bad money drives out good money. So there is a tendency to look for the easiest standard if you have a choice. And there's also competition between standards because then we have the argument of level playing field. So if somebody goes down, the other has to go down too. So I think it's a dangerous game potentially, and I think we should try to reach the need for a coordinated approach to reach high level, global standards, is I think proven. What also I think is a lesson we as an international accounting standards organisation have to take up is that you need always some kind of consultation procedure, even if it's short. The decision we made in October without any consultation, we've had so many negative comments on that, that we have to draw the conclusion that for the future, even if we take a short period of consultation, we need some kind of due process. It will be part of the constitution review to have a procedure for emergency situations, because you cannot always take a year when something pops up which needs immediate repair, but I think that the message we take at our heart is that we need some kind of consultation always. And these are the two things I'd like to stress from my part, which are of course at a rather abstract level. Maybe David can develop it longer on the response of the organisation to the financial crisis, the G20 meetings, etc., and I give you the floor.

DT Thanks, Gerrit. The response to the financial crisis really started well over a year ago, and was in the build-up to the March meeting last year of the financial stability forum. And the forum came out with three proposals as far as accounting was concerned. And we'd been involved in shaping those proposals before the meeting. One was to accelerate our work on off balance sheet issues, which we were delighted to do, because we dropped the discussion papers on each of these projects and went straight to exposure drafts. Secondly, there were concerns about the disclosures for valuations dealing with methodology and assumptions. And thirdly, there was the question of guidance for illiquid markets and how you got values in those. The G20 in November endorsed those comments, and additionally encouraged us with the FASB to move towards a single high quality standard. Several things happened. We set up the Financial Crisis Advisory Group, which I'll leave Hans to talk about. It's going to look at various issues. One of them, which I'll just mention just now, is the question of provisioning. There is a concern of pro-cyclicality. We've watched the... we've looked at the Spanish issue on dynamic provisioning. It's a lovely name. Nobody likes lethargic provisioning. But it's quite mathematical, it's related to the Spanish experience, and we're not sure how it will travel internationally. But we're looking at it. We agreed last week with our joint meeting with the FASB to do things on the existing provisioning models. This is for loans. Our present model, like that of the FASB, is what's called an incurred loss model. Something happens, and then you write down the particular loans. Now it doesn't mean that the company itself has gone bankrupt or has defaulted. That's the very last stage. But there is an indication that you're going to have defaults. Now that might be something such as, say, the oil price falls. That's going to lead to lay-offs in a certain area. That's going to affect mortgage loans and so on, so you start making provisions as soon as these things start to happen because your statistics show that this does happen. But we've discovered that the US actually provides earlier than we do in Europe, and the words are about the same, so something isn't happening. So we're not quite sure why not. We're going to meet with the firms to try and find out why, but one thing is, we may need additional guidance in IFRS if we stick with that. The other one we're looking at is an expected loss model which looks at losses through the cohort of loans, and this would be something... a different issue. You wouldn't look at the incidence of the loans, you would actually anticipate them. And that would be a case, for example, if you expected to get an 8% return on your loans, you'd probably charge everybody, say, 10%, knowing that the loss would amount to the 2% return. And your income would show throughout that period, if you got it right, 8% all the way through. Now, obviously, you have to decide how many percentage points are going to be losses, so that has an effect on your profits. If you get your losses up front, you will be carrying loans at a higher level than you can actually recover them, so it isn't without its problems this. And it probably can only be used by fairly sophisticated organisations, but we are going to look at it to see if we can do that, and we're going to do that with Sylvie's Basel Committee in dealing with that. Another question arises is whether that will be enough. Do we want a dampening down of profits in good times and a boosting of profits in bad times? Well, this is where regulation accounting start to move apart in the sense that our job we feel it is to show the economics, what has actually happened. Now we understand the regulators' need for stability and wishing to smooth out violent fluctuations, and the way that we've been looking at it is if the regulator wishes to do that, the way to do it is through undistributable capital reserves. Now what surprised us was the information from Basel that a lot of our banks had distributed almost all their profits over the last few years, either by dividends or by buybacks, and what could be done to stop that. And the obvious thing is you cut off a proportion of the profits and don't allow them to distribute it. And this could be a flexible matter that could be increased during good times and reduced during bad times. And we'll discuss various ways with Basel, and we're exploring this still, and Sylvie may wish to say more when I finish, is over whether we just do this through reserve appropriations, or whether we show a separate little statement which we could say would be called regulatory income which would take our net income, which wouldn't affect the income statement I may say, it's a separate statement, and from that you make these deductions and additions and whatever else Basel wishes to retain in an undistributable reserve. One suggestion was perhaps level three gains which have been distributed as well, even though they've never been realised and were based on models. So that could be used for compensation practices, for amounts of distributions, and so on as far as the regulator is concerned, but it would not affect comprehensive income. It would be an appropriation showing separately what the regulatory income would be. These are only suggestions and we're still working these through with Basel. Sylvie, do you want to come in at this stage, and I'll continue?

SM Yes, thank you very much. Well, my understanding is that here we are not discussing content, but process. So I will limit my comments to the process. I would say that we have been very happy to have those discussions. I understand that there have been, of course, not only us, but a lot of pressure against... well, on the accounting standards setters to take more into account in a more timely fashion losses than to wait until the last time and to have this pro-cyclical effect. And, of course, we have been quite puzzled to see that in the US under similar rules you do have different practices. So clearly, that's something we have to look at. But in terms of process, really it has been really very interesting to work together. It will be even better if you accept our proposal, but then... Thank you.

GZ Maybe this provisioning banking regulation is of interest of some other people around the table?

CB As a former banking CFO and CRO, I might be somewhat... a little bit biased perhaps. Also I'm a little bit more experienced. I have quite sympathy with what David just said that we have to distinguish between accounting and regulation. They are very close to each other. They are overlapping even, if you will, but conceptually also one has to distinguish a bit between accounting and regulation. Having said this, I must say on provisioning for loan losses, at the end of the day, I do have some sympathy quite a bit for a provisioning model which also takes into consideration expected losses other than just incurred losses. Loan losses have an unpleasant character that they occur in very bad times. If you look at the distribution over a ten year period of two loan losses, it's a very, very skewed distribution and one in ten you have a three standard situation, and in six or seven years you have a very benign situation. My view from a risk point of view is when you extend a loan, and even if the counterparty at this time is very good, or say you extend 100 loans, statistically, you know that over the life of the loan, this portfolio will show some impairments. And this is similar to a situation which we have in an insurance company when you underwrite certain risk. There is no possibility that you can escape loan losses when you do have a portfolio of loans. And now the CDS market also indicates to you that there might be... there are some loan losses. And, therefore, I do believe it is better to take up front into consideration that when extending a loan that you enter into a credit risk situation and to provide for this. I fully understand that it has to be a rigorous model. It should not be a model which can be abused for earning management or earning manipulation, but an insurance company also sets aside technical reserves for their underwriting risk and don't recognise in P&L on a pay as you go basis. So I would strongly encourage the ISB to have an open mind and to address and to work on this issue, because what you also see, David, if you look over a ten year period, in the very bad times, credit losses, that's interesting, have a tendency to be over-estimated and, therefore, you provide in the two worst years of a ten year period a lot to your credit provisions for a variety of reasons, and then some of that money comes back in good times. And this is exactly also what we don't want to have, and also gives a wrong impression to the market what the actual credit risk in the portfolio is. It's made transparent, you do it in the disclosure, you explain close provisioning is this, and recoveries is that, so the net is then in the P&L, but in the very good times, people look at the bottom line and that is it. And, therefore, I must say I've gone a long way and I've come to the situation that I have quite a bit of sympathy for a more statistical based expected loss model for provisioning.

DT Thanks, Clements. We are actively looking at, and jointly with FASB, because there has been a lot of criticism of what we've got and we have to learn from the crisis, so we are going to look at it quite sympathetically.

LS Can I ask David then about the expected loss model, how would that be different from the implicit expected loss model which was the basis of ratings of structured credit products? Because you run into problems of core relations, and core relations can overnight change from zero to one. You run into problems of the shape of the distribution. And a big statistic at the moment, the bell curve is not very popular. You get flat days and all that kind of things. So really, the rating of [unclear] was an expected loss model, and it didn't succeed very much.

DT Us, fortunately, Trustees aren't allowed to talk about technical matters, so I don't have to answer the question. But we are certainly going to look at all this, and Wayne's sitting at the back taking notes, and I'm sure he'll see you afterwards.

OF Well, a short comment; I agree with David that we should not confuse what was said by Clements about this regulation and accounting, and particularly accounting sophistication. In the case of Spain, the dynamic provisioning that you have been mentioning, it's important to understand that more than accounting sophistication, it had to do with regulation and supervision. The Bank of Spain and some of the Spanish banks has 30 people on a permanent basis supervising what the bank does. They are almost part of the bank. They work in the bank, not in the central bank. And, well, you mentioned, they approve the buyback, they approve the dividends, they approved how the loans are classified, and so it's a very, very strict regulation... sorry, supervision of the situation of the bank that explains to a large extent what has happened in spite of the real estate bubble that the country has experienced. But you know better than me the accounting system that they apply for this dynamic provisioning is very simple in practice.

GZ And then Charlie.

SM Yeah, very quickly, as I don't want to go into details and into content, that's true. We may prefer as banking supervisors to have as close as possible accounting regulations, financial regulations. There's also a third dimension that's internal management rules. It may be the case that it will not be possible because our objectives are different, but still in terms of process what we need to have, and I guess here accounting standard setters should help us in this matter as well as we should do our work as well, is to have a kind of audit trail between the information you have as an internal management, the accounting figures and the prudential figures, because otherwise I think it's very important to enhance market confidence to understand by how you move from internal figures to accounting to prudential ones. So I guess maybe it will mean that, and with the same methods, that we need to have an audit trail between the three types of accounts.

GZ Charlie?

CM Well, I know that I should just mention just the process and nothing else, and therefore I will say officially that there should be close cooperation between prudential regulators and the bodies responsible for stability, such as Basel, etc. I also recognise this; your very easily defended position that there should be clear differentiation between regulators and standard setters, but unfortunately, I have lived in the real world for a long, long time, and the real world means that we do not live in a political vacuum, and there is a direct... well, you have differential between the people who would say, well, we'll have the accounting rules like this, but regulators can do what they like and have it different.

Beautiful in theory, absolutely Utopian, but that's not the way Mark and other people interpret it. Now a lot of the difficulty with the early debates here, we had robust discussions about, say, the role of the EU and everybody else, a lot of it goes back to a feeling in the European Union in some member states and an absolute frustration with many member states with their belief of the unwillingness of the IASB to engage with regulators and central banks regarding these particular issues. Now let's talk about the real world for a moment, and I am actually a fan of the Spanish way that they have done it, and a fan of the dynamic provisioning. Why am I like that? Well, I'm old enough to remember when I was a young student that in my country that I know best, banks weren't allowed to publish their results in detail. Why? Because we felt if everybody saw the reserves, etc., it would create maybe a run on the banks. That's... I've lived, as I say, within the '60s, and we didn't produce our full accounts. We weren't obliged to do so, and building societies and other institutions as well, and we've moved a long way from that. But strictly speaking in the real world, what the Spanish did, which has resulted in them for lots of reasons, not just to do with the interpretation of IFRS, for example, the banded provisions, for other reasons that I accept, that there is that the Spanish regulator didn't allow, as I understand, the Spanish banks to involve themselves in products like SIVs, etc., etc. He did all that, and there's a lot of people... many other regulators have more than 30 people in every bank. I'm sure there's 30 or more people in every bank in the country I know best. It didn't stop them going into difficulties that they are now. But think of it like this. The Spanish have held up despite their economics situation with perfectly strong banking. Of the banks here, none are owned by certain Spanish banks because the regulator did it in a certain way. But funnily enough, I should have actually been taking action over the last year on infringements proceedings against the Spanish for allowing the Spanish regulator to not to allow his banks to go IFRS route. I should have been prosecuting him for being responsible and conservative if I'd been thoroughly doing my duty, because all other countries in the EU had adopted IFRS and did it in a proper way. The Spanish regulator said no, and we didn't go down this particular route, but that was the next step. And wouldn't I look bloody well ridiculous going down with the person, the regulator who has managed his affairs in such an order that he ends up at least with a banking situation which is pretty... well, at the moment you can't say next week, but it's stood up until now in pretty bad times. Wouldn't that look absolutely ridiculous? So we can't operate in a political vacuum in this situation. Now those that think that we can should consider this. We could have the most beautiful accounting situation in banks and institutions, but we'd have maybe no banks. Well, that's a little bit of a problem, because with them all, like we won't have anything to regulate or do accounts for. Now, since we're in the City of London, there was a very famous comedian here one time called Marty Feldman, and he's dead maybe 25 or 30 years. He was the guy with the big eyes, and in the country I come from, we didn't have our own television station, we always looked at the British television. And I remember particularly a sketch that Feldman did. There was a guy here in London who became the first 80,000 sterling footballer this long time ago in a transfer. Then someone went for 110,000. So Feldman did a sketch one night where he was a footballer being transferred, and he was transferred for 100,000 and then 200,000 and 400,000. And then lo and behold what happened, he became too valuable to play football. And it always struck with me that if you think it out to its logical conclusion, we will have such a perfect accounting thing without it related to reality when we wanted anything to regulate our account. And we in the European... the member states in the European Union have a high degree of frustration. The changes that they've demanded over the years haven't been followed through. Now I can go through them individually and one thing and another, but the one thing is that, and this is straying over what the Monitoring Board is supposed to do, but I'm not... like since other people have strayed over into it, I'm going to stray into this particular sphere as well. I think in setting these particular standards, and that's why I spoke about road testing in an earlier contribution, like we cannot live in a Utopian ivory tower in these particular issues.

CB Three observations; the term audit trail was mentioned. I fully agree. The basis for all reporting within and outside a firm has to be the information which is provided by accounting. That is the basis. If you do have differences as far as management accounting is concerned, you have to have full transparent reconciliation. And the same you can apply for regulatory purposes. The starting point, the basis, is the accounting numbers, and then you fully reconcile and that is what was mentioned with that audit trail, and one must not have different sets of numbers without an audit trail, without a full reconciliation. That is clear. Number two where I'm concerned is about this notion of now, of different quality, of different quality of earnings. It was mentioned these are earnings from level three assets and therefore they do not qualify for distribution and they have to be set aside for reserve A, and if they are of a different quality again, then it's reserve B and so on.. And we should say all results which are derived from the proper application of accounting standards are revenues, costs, income, and we cannot qualify. If the regulator says I want to have a higher capital ratio under those circumstances, this is a different matter, but to start with we have different kinds of quality of earnings is really not helpful. And thirdly, the game is not just between the firms, the standard setters and the regulators, there is a market. And, for example, if you take the financial industry with all trade in aggregate, 40% of tangible book... of book value, 40, 50, 30, it's about that, most of us don't trade at full (unclear). And why? Why? So what is the point, even if our equity would be higher by 10 billion, it wouldn't have an impact. And the financing, the funding costs, are also not related anymore, because people are concerned about the quality of balance sheet, about risks not fully recognised in the balance sheet. It is a lack of credibility. And, therefore, if financial institutions break on certain accounting standards, and they show then it would profit the result, it's not what we want to be that the funding costs go down and capital can be raised, the result is that we create or that we further undermine the credibility. And, therefore, I only say I know all these constraints, but we also have to keep in mind that we maintain the integrity of our accounts so that we can ask the markets, you can go to the market, you can give us full credibility because these, the numbers, are the numbers and these are the right numbers.

GZ Bob?

RG Perhaps I misunderstood Commissioner McCreevy. I thought he said that the reason Spanish banks had been more successful than others in navigating the financial crisis was that he had permitted them to violate accounting standards. Was that right?

CM I didn't permit it, they just did it. But logically...

RG Well, you didn't pursue them.

CM We hadn't arrived at the situation of bringing infringement proceedings against them, but logically, that's what I should have done.

RG Well, I just... I believe in the US where we've had banks that have had difficulties navigating the financial crisis, my own personal view is that they would not have been more successful had we allowed them... our regulators allowed them to violate accounting principles. I just don't think that's true, and I don't know where the evidence is. In fact, markets work best when they have confidence in the numbers that institutions, businesses publish, not where they have no confidence in those numbers. And you can't fool the markets. Clements just said that, and surely that's correct. So I don't believe, whatever the reason is for the Spanish banks having navigated this crisis better, it wasn't that you didn't act to prevent them from violating accounting rules.

CM They didn't implement IFRS and our regulations said from the 1st January 2005 all publicly listed companies had to implement IFRS. The Spanish regulator did not do that and he survived this... his banks have survived this crisis better than anybody else to date.

RG I don't mean to be criticising you for acting or not acting, but I don't think that's the reason they survived better, that they failed to honour accounting rules.

CM No, I'm making the point is that the rules did not allow the dynamic provisioning that the Spanish banks did, and the Spanish banking regulator insisted that they still have the dynamic provisioning. And they did so, but I strictly speaking should have taken action against them for doing this responsible set of actions. That's the point I'm making is the ludicrousy in my view of some of these particular rules. The Spanish... and it's worked pretty well for them.

RG But, Charlie...

HH Every banking regulator in Europe could have demanded his own banks to have more capital than what they did. What in fact happened was that we had Basel criteria that said that the banks had a capital base of 10% while they actually had a capital base of 2.5%. And the Basel criteria were at a certain point completely out of touch with economic reality, but it could not... it would not have avoided national banking regulators from implementing higher requirements than those required by CRD

CM I don't think you're correct. What had 2.5% was equity; an equity base. That was to say it was Tier 1 capital. I'm not going to defend the Basel Committee, but what it had was equity of 2.5% or thereabouts, but had Tier 1 capital of... Tier 1 was about 8% of the case, but what you're talking about is not Tier 1 capital, it's the equity.

RG No, but there was an incredible divergence between Tier 1 capital ratios and the actual gross equity ratios which were unreal, and that grew so far apart that that's the reason why these problems occurred.

CB In this, I must... you are right. They had an additional reserve, an additional allowance on credit. It went to P&L and they now can release this against credit losses, so they have an additional reserve, and they can go to the market and say, don't worry about me, I...

CB Okay, through P&L, so we have two cases. In this case, we have an additional reserve, and under IFRS, you are not allowed to have this reserve in the accounts. But what was discussed is a different thing, and this is not recognising mark-to-market losses, and this is a different thing. And therefore we have to deal with two things. Is it permitted to have reserves, or is it necessary and are you obliged to recognise all losses. And they have two different implications as far as the markets are concerned.

UM Because what I think, Charlie, also is implied is that because they didn't follow the standard accounting practices, they show less profits than the real ones, and they distributed the less dividends. So in that sense... perhaps they didn't show... And they could be criticised from a purist accounting point of view, because they were not showing the real profit they were making.

CM No, they could only be criticised that they didn't follow IFRS. They did it like the way they'd done it for the previous 30 or 40 years, but if they had strictly speaking been following the IFRS as their public companies were supposed to do, then they would have been in the same bad situation as... [overtalking].

LS Commissioner, Italian banks follow the IFRS. They followed the IFRS and seem to be all right.

CM That is the first point I made, and the second point I made after is that this notional Utopian idea that you can differentiate between what regulators want and the accounts are for the public investment.

GZ That's what they're doing now.

CM I don't go along with that in the real world, but you have, as my friend Clements has said anyway, yes, you're supposed to have a reconciliation across from one system to the other, but in the real world when people look at these particular figures, when bank A produces its results, while there's looking at the headline results and the headline figures there, we have a different kind of regulatory capital in this particular area, and this is causing some of the confusion at this particular time. And my point is that we have to be realistic about we're living in the real world here, because what we have allowed, it's not the accounting rules that's brought on the financial crisis, it's not any one singular thing, but what some of these new rules have done is exacerbated the situation, and that's the point I think most people outside of accounting land would agree.

GZ But in the same real world, Charlie, regulators always made amendments to the accounting system. For example, goodwill, it has to be activated under IFRS, and the first thing Central Bank is doing, skip the goodwill and deduct it from equity. So they can do it, and they do it practically. So the Spanish bank could have done it also in another way than just saying, well, don't apply IFRS. That's my opinion.

SM Thank you. Well, I think I have to say something for the Basel Committee and all those credits. So that's true, there has been a lot of leverage builtin the financial industry, and that's true that the weighted capital ratio did not help in a way, but you have to differentiate between the capital level and the provisioning level, because clearly, and we have to admit, that it's not us anymore who fix the capital the market wants. That's the market. And if you look at the figures, the figures are much more higher than the minimal requirements because the market is requiring that. Then is it helpful? Well, you can look that you have banks who have very high level of capital, and may face a lot of difficulties. So that makes the distinction of the usefulness of having high capital ratio, which of course we like, and reserve on which you can draw upon during bad times. And clearly that's I think what the Spanish banks made. It's not to say that this model is better. I guess the fundamental reason is that, and that leads us to the financial reporting issues, when if you want to enhance confidence of market, if you want to enhance the quality of financial reporting, you have to report the situation of your company I guess. Well, that's our view in the Basel Committee at least; not as it is today, but with everything, every losses which are already embedded in the portfolio. And I guess that's what the system does, and that's certainly why... at least that's our feeling, that those banks were better off during the crisis because there had been reserves which in fact were covering losses already embedded in that portfolio on which they can draw upon when the crisis occurred. And that's the kind of discussion we have with the IASB board and staff, and clearly, that's why we would like to have a better reserve and a better taking into account, maybe not all expected loss, but maybe at least incurred but not yet materialised loss. And in fact, in a former IASB proposal for IAS 39 in 2002, we very much liked what there was in that 2002 proposal to take into account those embedded losses in the portfolio.

GZ How nice to be chairman of a group where we never talk about substance, only about procedures.

SD That was a very interesting exchange. Just a few observations, and my observations should be taken with the understanding that I have a great deal of sympathy, as Clements described, to the concept of expected losses as opposed to just incurred losses, because I do believe that there is some methodology there that can create not stability but transparency. And so my two observations, and Charlie, with great respect to your world of having to struggle through the politics and the reality, there are really two things that we... I will speak now as a member of the profession, not as a Trustee, we have first an obligation to investors to create transparency what is the economic reality of the accounts. And if you confuse the economic reality of the accounts with stability or setting up reserves in good times for bad times, the one thing we know is the investor will not know what's happening. And there are different ways this may be reflected, but I am a believer that expected losses may have a role to play in reporting. I'm also a believer that those banks that survive this crisis did not do it because of some funny reserving approach, it's because they made very conscious decisions, or the regulators made conscious decisions to avoid certain investments. That's what happened in India, that's what happened in Spain. It was not about reserving. It was about staying out of asset classes. And in the end, whatever accounting we create, we are not... as an accountant, not as a Trustee, as an accountant, if we're not serving the needs of the investor and creating transparency, we're irrelevant.

JM Thank you. Just a clarification that as a bank regulator, Chairman, you said that the bank regulators can always change the rules; like you said, the goodwill and things. But it's only for the prudential reporting purposes only, right? So they can't change the accounting standard at all, at all, because this is for the investors' information purposes, users' purposes, and also that those accounting rules should be applied to across the board manufacturing industry, service industries, and banking industry and other financial industry people. So that's a sort of yardstick which you can't change by any means. On the other hand, of course, the bank regulators can change some sort of marginal rule, the provisioning, and marginal rule for goodwill, whether they should be deducted from the Tier 1 capital, or whatever. But it's only that for the prudential reporting purposes. And that is held within the discretionary power of these countries by bank regulators. That's one point that I would like to clarify. The second point of the clarification is before jumping into the discussion of the level of the capital, or whatever, I think that the starting point is that the risk control, risk management, risk valuation techniques, I think something must have been wrong for the calculation of the risk so that the banks reached the wrong level of the required capital, which is much smaller than the real risk. So had the bank calculated in a very correct way their risks, whatever the subprime or structure of the credit, whatever, then they must have reached this level of their required capital. However, something must have been wrong with we think this calculation, the mechanism. Artificially, intentionally or unintentionally, I don't know. So they concluded that this level of the capital was required, so this should be enough, or whatever. So it doesn't mean that 8%, or 10% or whatever, so of course, then after that, we can discuss about raising the level of buffer, or minimum, whatever, but I think that we have to discuss both at the denominator and numerator level at the same time. The denominator is as risk capture, whatever,and also the level of the capital which is a numerator. Thank you. So that's the second clarification.

GZ Thank you. Last in this row is David, and then of course the other David, and then I want to try to close this subject of accounting and bank regulation.

DS I think one of the interesting things here is if you look at the level of protection to investors, creditors and general users of financial things, is both reserves and capital. So in a way, we're talking somewhat academically about how you want to make that split between what shows up in provisions, hence into reserves, and what level of capital is required. When you think about expected loss models, they're going to have some assumption about the level of frequency and the size and timing of losses. I think, irrespective of what decisions you make in those dimensions, you're probably also going to want to say, should capital cover us for what frequency of the 100 year storm? Is it really a 100 year storm, a 50 year storm, or whatever. I think at the end of the day, this isn't just accounting. This is how accounting intercepts with the level of capital that people are going to require, and maybe some of what we need to do is just make sure we're clear about what is the basis for provisioning, i.e. reserving, and what is the basis for determining capital to deal with risk concentrations and portfolios to deal with uncertainty of expected outcomes, and all of the other things we try and model, because if you actually look at the regime that banks have operated in, the way risk based capital is calculated was attempting to get at a risk assessment of credit losses when models were used, and clearly with the benefit of hindsight they didn't stand up very well. Don't forget, that can be the very same basis of expected loss modelling, so I think as you pursue this work, we probably need to make sure we're very clear about what we're trying to do between method around reserving, method around capital, and both have a place in this world. We just need to make sure we're very clear about what we're trying to do with each.

GZ Sylvie, with a cri du coeur.

SM We have a very clear answer for us. Reserve and provision, that's for expected loss, capital is for unexpected loss. And in an ideal world, expected loss will be taken into account in accounting standards as well, because as Junichi said, that's for financial reporting and that's for investors and everybody. So for us, expected loss is reserve, is accounting. Unexpected loss is capital, and that's our job.

DT I think, anyway, that what David and Sylvie have just said is probably the Board's view as well. We want a measure of what the losses are going to be. The losses that have been incurred didn't seem to work very well, and we're now investigating the expected loss model. Where I disagree with you, Charlie, is the point that Sam made, that the real problem we had was banks' risk management failed. They got into very risky assets and as they rose, they distributed the profits that seemed to be coming from these, and I don't think any measure of expected loss would have picked up the losses they eventually had. They're colossal in some of these CDOs. And we're talking huge of tracts of them disappearing, not just some 10% or something like that have gone. That wouldn't have been picked up, and if the Spanish banks had gone into them, they'd have been in big trouble as well. The capital simply was too low to deal with what Sylvie calls the unexpected losses. If you've got assets out there of 1 trillion, and capital of 50 billion, it doesn't take much to blow it away, and it got blown away. And that's exactly what happened. Simply putting through massive unexpected loss reserves or provisions is great in damping down good times, but just imagine the writs, and your lawyers, Charlie, wouldn't be going on holiday if you started stuffing these in in bad times and showing profits when the banks were collapsing. That's the problem. So I think Sylvie hit the nail on the head. What we have to try and do is provide for expected losses. Now how we do it, and we're going to explore it, and it's complicated and we have to try and get it right, but the other aspect is that reserving for the unexpected losses. And it's dampening it down in good times. Let's take a bit of that and don't let them distribute it, and then you've got this flexible capital that you can let go in bad times and re-sell it. And that's what Basel and ourselves are trying to work to. So I think that's where we're trying to get to, and then hopefully we can both get what we want, Charlie.

CM I would never say that it was anything to do with accounting that caused the financial collapse, nor was it just credit rating agencies, nor was it a whole variety of things. It's a combination of a whole lot of things coming together that has caused it, but I'm just trying to deal with the point how accounting has played a role in all of this as well, the same as all the other actors in this. Now it shouldn't take a mathematical genius to have worked out that if the equity in a financial institution is about 2.5%, and our leverage of that is, say, 40 times, say 35 or 40 times, I know of no economic risk model, and I have a little bit of experience of this in my past life, that can predict loan losses to an accuracy of plus or minus 3%. So if you have a loss, say, of 3%, you've wiped out the whole blessed capital of the financial institution. You don't have to be an Einstein in mathematics to be able to take that onboard. So there are issues to do with financial stability and the financial ability of the Basel Committee for all of this to be addressed. The same in here and across the world as well. I've the height of respect for Sam, because the firm he represents I had a long association with them in a previous life. But he did make the point that the accounts should... he used the phase, the economic reality of the accounts, and I would agree with that. But in the City of London, at least in the last year, a major bank here produced profits of so much, of which nearly one quarter was as a result of a technical kind of add back due to the mark-to-market situation. In fact, the worse off they became, the better the profits were going to become. Now that is counterintuitive. It shouldn't be. That shouldn't be. And that is the result of fair value accounting. Of the top of my head, I could say the profits reported were something like 3.2 billion, of which 800,000 was this particular division. So the logic, like the story I told you previously, if they kept getting worse off, the profits would keep going up. So finally, you had the ultimate situation where if they were bankrupt, they had the best profits of all, and that is counterintuitive I say, at the minimum. And these issues have to be addressed.

DT Well, that leads me into my next point, because they are going to be addressed, and this has been... you know, we've heard today, as Bob said, don't miss an opportunity of a crisis, because one of the big problems we've had is actually getting our hands on IAS 39 without everybody jumping up and down and shouting about it. That was my introduction. Can I go on to the rest of the...? Well, I started off by saying there were things we were asked to do by the Financial Stability Forum. I just happened to mention provisioning, and that was the end of that. But we were asked to look at the issue of illiquid markets, and we set up an advisory group which consisted of representatives from 20 major institutions. And these were the actual people who did the valuations. We then got the auditors, the actual auditors had to justify the valuations, and they had about seven meetings over last summer, and they came out with a draft report in early September and finalised it at the end of October. That was very well received. It made it perfectly clear if a distressed sale took place, you did not take it into account. You had to leave it alone. We asked them a couple of months ago whether there were any other issues that we had to look at that would actually help us to amend or expand the guidance. We've had one or two small things in, nothing major so far, but we are keeping that under active watch. Some of the lessons we learned from that were that we needed to enhance the disclosure regarding liquidity risk, and also we brought in from the US standards levels one, two and three of disclosures, level one being market values, level two being market values adjusted for your particular instrument, and level three being models and showing the gains and losses and how the assets at fair value were within these categories. So that's ongoing. We're looking at that there. The issue of off balance sheet, while fair value and the valuations have got a lot of attention, off balance sheet has been one of the major issues of this crisis, and I think we were all fairly surprised when some of these structured investment vehicles came flying back on to banks' balance sheets, even though the banks had said there was no connection, they were taking no responsibility. They came back for reputational reasons and litigation reasons. We've issued an exposure draft last December tightening up our consolidation proposals, which were pretty tight already. I think I mentioned in the open session this morning that when Deutsche Bank moved to IFRS from US GAAP, another 200 subsidiaries were consolidated, mainly these qualifying special purpose entities we believe. We don't have those, but nonetheless, we've still tightened our proposals, and also put in disclosures to say, well, if you weren't quite certain if you controlled it but you thought you didn't, what investment have you got in these vehicles, and what is your maximum loss? So the off balance sheet risks I think are much more clearly laid out in our draft standard, and we hope to finalise that this year. Yesterday, we issued the draft standard on derecognition, which is the securitisation proposals, and it's taken a fairly tough line in line with US practice; not quite the same but very similar. And there was a big argument. We've tried to simplify how we did it. Basically, the criterion is if you have continuing involvement in that instrument, the question then becomes, can the person to whom you have transferred it, can he transfer it on? If you, for example, have a call option on it, it might be easy to transfer if it was something like a treasury bill which is easily replaceable, but if it was this building, he can't really transfer it. So you probably haven't sold it, so you keep it on balance sheet. There's an alternative view saying all we've got is a call option and we value that, which would mean lots of these things go off balance sheet. We haven't adopted that approach, so these things will stay on. If you want to get rid of it, cut your connection with it and you can take it off balance sheet. FASB have agreed that they will work with us on this. They're having to deal with their own standards at the moment. They're fixing things on qualifying special purpose entities and one or two other issues, and then the idea is the two boards get together, look at the responses we get, and they help us finalise our standards which they will issue as exposure drafts. So the idea is we end up with exactly the same rules in this area. We're also looking at simplifying IAS 39. This is something we've wanted to do for some time. We've never had a major look at 39. It was one we inherited. People think we wrote it, but we didn't. And basically, it is far too complicated. I've often said, if you understand 39, you haven't read it properly. And we have to look at it in the sense that it has four different categories of financial instruments, with different accounting rules for each of the four. We have trading, available for sale, held to maturity loans and receivables, and we believe after discussing that what we should do is simplify this by collapsing them into two categories. One is fair value and the other is amortised cost. And it cuts away a lot of the differences between the categories. We can get rid of all the tainting rules, because if you sell out of the costs category, you just simply show the gains and losses, so if you're stuffing income by selling cost held assets, it's obvious. How we present the ones at fair value we could discuss. You could have some in trading, some shown as long term, but the rules would be exactly the same so it would be no difference. We could have one impairment rule instead of three; much simpler to disclose. So that would be much more simple to deal with, and that's what we propose that we will try and deal with in the next six months. We've got FASB to agree to come in to try and get a new standard for USA as well. Our timetable probably wants to be quicker than theirs. They've raised the question of whether instead of amortised costs, should they use present values? That strikes us as something that will extend this much longer, and our initial preference certainly is to stay with amortised cost, and that's something we have to debate with FASB. But the idea would be: never mind these little fixes, just go for the big fix and try and simplify and clear up this standard as best we can. We had other issues. We had the reclassification issue in October. We're rather not have reclassified. We'd rather FASB had change to no reclassification, but there was no time to do that and we had to change to their standard. Other issues that were put to us was reclassification under the fair value option, the impairment changes. This we want to sweep up into this full revision of IAS 39. We think it needs a root and branch examination, and the issue Charlie mentioned as well, the gains on own debt, we're well aware of that, and that's something else that's thrown into this as well. So this is something we'd like to come out with proposals within six months or a bit longer, but we need to do it quickly. And what can't be done is side tracked. The joint round tables we had with FASB towards the end of last year which we held in Tokyo and New York and London, made it clear in this area we should work with FASB, we need full due process, and actually, we need to do this broad examination which is what started us looking at it. Don't do little fixes. So that's what we're intending to do. Now we have another little problem in the sense that a couple of weeks ago, FASB were forced by the US Congress to put out two staff positions. One reverses the assumption that in distressed markets you look to see if it's a distressed sale. If it is, you don't count it. They assume they're all distressed sales, and only if you can prove it isn't do you use that value. I think our reaction to that is that's giving them a choice of two values. If you like the value, clearly, it's not a distressed sale and you'll go out to do your damndest to prove it isn't. If you don't like it, you'll just leave it alone and use a model. That has had quite a bad reaction we gather in the responses that FASB are getting, and we've put it out for comment, and we've asked people what to do, and we will have a look at that, but that would be another major distraction for us. The other issue they've dealt with is on impairments. If we were to adopt, it would not be a minor matter. Our rules on impairment are different from FASB's, in most cases, not all, but most reversals. If the impairment turns out to recover, you write it back. FASB doesn't allow that. FASB also deals with what they call securities, which runs through available for sale and into held for maturity. The write-downs for those are at fair value. We don't do that for held to maturity. We use a discounted cash flow method. So we'd have to rip all that out and probably cancel reversals. The other aspect of it is they have brought in if you think you can recover some of the asset by the time... you don't have to sell it rather, and you can hold on to it, then you only write off the credit aspect of the loss to profit, and you take the other bit to other comprehensive income and then amortise that over its life. This is starting to get complicated. If you can't hold it, then you write off the full fair value loss. So this is not a minor thing for us if we were to do it. This would be tearing great chunks out of 39 and would take months and be subject to dispute. Our view is we should crack on and try and fix this standard and have done with it, and put on a very tight timetable. We promised the EC that we would try and do this within months, not years, and that is our target. And the more we get distracted with these sorts of things, we just won't get it done. So that's our general reaction and what we would like to do in the future. I think that's really... most of it is about the crisis. Any other issues we can discuss?...

GZ We go for the big bang, for 39 now. I'm interested whether there's sympathy for that idea. There is sympathy for that idea, yeah? Okay, well, it was a good point there. Any other questions, comments, or...?

CM The G20 is making and has made, and will be making various recommendations in this particular area as well, and we'd like, say, the IASB to publish a timetable outlining what their timelines in this particular area will be as to what they recommend. I think it would be useful. Secondly, we would like the... I'd like to make this particular point. There's a high degree of frustration, again in the Commission and in my services, as that we would think... the target is the slowness of the response of the IASB to our particular concerns, which we raised in the letter with them of last October, and it has taken a considerable amount of time before we had any kind of detail. We've got to now the end of February, and there's another one there recently. And we would like our concerns to be dealt with from the... our EU Commission concerns to be dealt with with the same speed that the concerns of other actors are in this regard, somewhat at least within the same couple of months, rather than having instantaneous responses to some particular requests, and months of delay and ignoring ones coming from the EU Commission. That generates a lot... it further makes more hostility in this particular area.

DT Well, Charlie, one of the things we've been criticised for was acting within a week over the reclassifications. We have been slaughtered in America for that. They were very unhappy about what happened, and we've never acted faster. The information from the round tables quite frankly was none of these requests from the Commission were absolutely imperative. What we ought to do is fix the standard, and actually why we've been over the last two or three months developing what's the rough cut for the standard, and that's broadly what we've been announcing today and we've been discussing with FASB last week. This is what we have been told that people want us to do, because we asked the markets and the markets told us, don't do it, fix the standard.

CM I have to point out, we don't feel like that about it in the EU Commission.

DT Well, Charlie, we went out for due process, and that was the answer we got very loudly and clearly, and that was in Tokyo, New York and London. And it was a very broad spectrum of people that gave us that answer. It was very clear.

CM We'll have to differ.

GZ Well, that's one of the possibilities in life, and let's enjoy life anyhow. Are there any other comments or questions on issues relating to accounting and the financial crisis and David's report? If that's not the case, then I'll ask Hans to inform us on his Financial Crisis Advisory Group.

HH Yes, thank you, Gerrit. Actually, I can be quite short, because what you saw just now was sort of a replay of the kind of discussion that we have all the time, and quite frankly, I had never expected accounting, I'm a foreigner to accounting, and I had never expected it to be so intellectually... that it has intellectual entertainment value and that people can actually get emotional about it. That is also something that you would not expect. But to be serious, these are very good discussions that we have of very high quality. We have a group of 18 senior leaders with broad international experience in the financial markets together, among whom people are like Tommaso Padoa-Schioppa and Jerry Corrigan from the investment bank world, and it's really a mixed bag of people. The decks are not stacked in favour of the current accounting standards. There are a lot of critical thoughts going around in this group, and that makes for a very interesting discussion and not for easy consensus. And we are not there yet. What there is some consensus about, we have been discussing fair value accounting, of course. There is a consensus that this was not a major cause of the crisis, although there are among us that feel that it did reinforce the crisis, while others think it didn't play any material role. There is consensus that, as David already mentioned, that where accountancy actually did make a contribution to the origins of the crisis was in the insufficiently rigid rules concerning derecognition and consolidation. And so it is absolutely necessary that there is a considerable bit of tidying up going on in that field. And it is interesting that the whole public discussion is centred on fair value, while this was probably much more important to the crisis. But that is being solved in consensus. We also broadly feel a great deal of sympathy for the economic philosophy behind dynamic provisioning, and when I hear David and Sylvie talking about the expected losses model, I even, if you look at it closely, dynamic provisioning is an expected loss model. And so we might be much closer to consensus there than you might think, but of course, this is technically an extremely difficult thing to do. But generally, there is sympathy for methods, whether it is dynamic provisioning or deterioration of an economic cycle reserve which has been sketched very well I think in the Turner Review, that something like that is probably necessary from the point of view of stability, and that the accounting profession, the accounting standard setters should do something to make that clearly visible, not just as a gesture to the regulators, but also to create perhaps more transparency to the investor that it will also be easier for the investor to look through the economic cycle. But this discussion is still at a very high level. It will not be so easy to reach consensus on that, but if I see how the public discussion is evolving around this issue, this might very well be possible. So a lot of discussion is going on about that as well. The final issue that we have not discussed at length yet but which we will retake, and probably after the G20 might indeed be forced to re-discuss, is the whole issue of independence versus accountability, due process, and accountability of the standard setting process. We have only just started this discussion, so I don't know where it will lead, but as I said, it's probable that the G20 will come up with some suggestions there as well, and I suppose we can take them up in this group. So all in all, I think... we hope... we have had three meetings thus far. We will have a meeting in April and a meeting in July. And we hope to come up with a report in July, and I think it might be wise if we then remain dormant for a couple of months and then see what is going on in the actual work that the IASB is doing and that we get together again later in the year to take a second look at what actually has happened. So that's basically where we are and how we wish to proceed.

GZ Thank you. Do you still do any supervision at home?

HH I leave that to my people.

GZ Okay. Who has questions or remarks?

PT What do you consider the most urgent problem that you want to solve?

HH To tackle? Well, you know, to tell you the truth, I wonder how urgent these things are. Well, if you look at... I sympathise with the people, because I have the same feeling as well that feel uneasy with fair value accounting because it is completely clear that the efficient market hypothesis, which was underlying both regulatory and perhaps even accounting practices in the last decade, that the efficient market hypothesis is completely discredited, and that markets do indeed go mad and that probably there is under-shooting and over-shooting in the prices of assets and also of financial assets. And although it's easy to overestimate it, it is probably true that in the whole of financial assets, there is some under-shooting of value at this moment. But if you look at the main assets of banks, which is the loans and receivables, there we have probably a huge under-shooting of the true losses that are still hidden there and which will come out as a result of the recession. So I think the net effect of accountancy standards on the whole balance sheet of a bank is probably neutral or possibly even too positive since the amount of assets held at... measured at historic cost is much higher than the assets valued at fair value. So the people who... and it's interesting that the two main issues that are being addressed now, fair value accounting, where people hope that it will result in higher value, and the other one is the dynamic provisioning economic cycle reserve which people hope will lower values, well, they cancel each other out in the short run so I think you should not have hope that a simple change in accounting rules would lead to a much more rosy picture of the balance sheets of financial institutions. And therefore, I think it would be wise to act as speedily as possible, but not to forget about due process.

GZ Tom?

BC Well, I think in what you said, something which is very important is that as some reminded us, we want to give a picture of the economic reality to the investor. And as you said, the economic reality includes the cycle. And probably the main mistake of the past was the new product but no cycle. And economic reality is that you have not made any money on a loan until it's paid back. So whether you put part of a gain in the beginning or at the end, it's two different readings of the economic reality, but there is not one which is more economic reality than the other. Well, actually, the economic reality would be to wait until everything is finished to recognise the gain. So anyway, I think this idea that the cycle is something that we should get into, you know, the reality we show to the investor, I don't know how practically you transform it into an accounting standard, and that's probably pretty tough. But I think it's an important concept that you've been mentioning.

GZ Okay. Thanks again, Hans. One of the subjects also on the agenda would be are there any interesting developments at the regulators which may impact us. Well, it's in my sheet. I don't know whether you have the same agenda, but it is said, report by Monitoring Board members on relevant developments in the regulatory environment.

GT Perhaps, Chairman, I might start just about the developments in IOSCO level, and then go to Julie for the specific accounting related developments, and I won't take much time. It was really to give you a sense of some of the developments in non financial reporting issues that might be relevant for your work. IOSCO's work most recently has focused very heavily on this issue that we were discussing previously about special purpose vehicles and off balance sheet issues in relation to the perimeter of regulation; the shadow banking system, where should regulatory principles extend where perhaps areas have been unregulated or under-regulated in the past. We set up after the G20 leaders' summit last November three special purpose task forces, two of which were specifically directed to this issue of the perimeter of regulation. One of those is on unregulated markets and products, and it's focusing on securitised products and credit defaults, the credit default swaps market as examples of two unregulated or under-regulated areas. On the disclosure side, I think it's quite interesting that it looks like this particular taskforce will be reporting fairly soon publicly, but some of the options that we're considering in terms of transparency go to both transparency on the selling side and on the transparency and due diligence, both on the selling side and on the buying side. On the selling side, both to make available the information that investors might need to make a reasonable decision about the risks involved in the product, but also to encourage for sellers that they have a responsibility to consider the risks themselves in producing a product to try to address this issue of the misalignment of incentives that seem to be so evident in the excesses of the originated distribute model that gave rise to the initial parts of the crisis. On the buying side, very much an emphasis on the types of due diligence processes that investors, and in particular, investment managers should follow in order to come up with a reasonable investment decision. And it is interesting that in this area, if you look at the type of ordinary due diligence that an investment manager might do, if that was followed to a logical extent, and it not always is, it does give you pause to think, that would solve a lot of the issues about very unsafe products being sold because most of the typical questions that investment managers ask themselves are about the opacity of the product, are about the underlying assets, are about the security of the income stream and so on. On top of those issues around the perimeter of regulation, we are also continuing our work on credit rating agencies. Of course, we updated the IOSCO code of conduct last year, and going to the two critical issues I guess, about the management conflict of interest within the existing credit rating agency model, and the issue of quality of ratings themselves, I think the code has rightly been criticised for the fact that it is a complier explained or a voluntary code, and you're seeing in a number of jurisdictions, notably in Europe, measures to implement a direct regulatory regime. But in most circumstances, basically building on the consensus, or we have the feeling that it's building on the consensus about the content regulations, perhaps extending it in some regards. Julie might like to speak a little more on the more accounting aspects.

JE Sure. Thanks, Greg. As part of my responsibilities at the ICC, I chair IOSCO's Standing Committee on accounting and auditing and disclosure. And so let me just make three points about the work that we're doing that might be of interest to you. The first actually relates to offerings of asset-backed securities, which is an area where IOSCO has never gotten together and tried to figure out what actually would be the right disclosure package for investors in one of those offerings to the extent it would differ from the right disclosure package in a corporate offering. And so we are in the process of... our first conclusion was, yes, it should differ. We couldn't get any mileage really out of our existing principles of what that disclosure should be in a corporate offering, so we're starting from scratch to develop what's the right package of information in an asset-backed offering in the public capital markets, and we expect to present that for public exposure and comment at IOSCO's annual meeting in June. One interesting thing we found out is that actually from jurisdiction to jurisdiction, the degree to which security regulators' mandate actually covers these offerings differs quite a bit, so that was a learning experience in terms of trying to find consensus when some securities regulators don't have much of a remit at all in this area, and others do. The second point I'd make is... second and third are closer to actual the IASB's work in accounting. One is we've chosen to participate in the work on the credit crisis with respect to financial statements reported under IFRS, not by trying to run the IASB or do their work for them, but rather to participate closely with them. So we've participated in all the round tables, write comment letters and all their proposals, are on their task forces, so we're sort of a... it's a bear hug type of approach I guess but a friendly one. And so we've been generally supportive of the work they've been doing. I mean, we have our comments and suggestions like everyone does, but we feel like we've been on the ground in a real time basis to try to get our view there, and so that's been our tactic. The third thing which goes to the more strategy question David was talking about, which is how do you deal with financial instrument accounting big picture if what we have now, IAS 39, isn't an optimal standard complexity-wise or otherwise. We actually wrote our comment letter back in October to the IASB on this question when they solicited. Back then, the crisis was limited to a couple of investment banks I think. But they solicited comment on what's the best way forward to fix 39 to put it in very mundane terms. And we wrote a comment letter then that said, yes, we're supportive of long term work toward an ideal standard, but predicated on there's some short term fixes that need to happen first. And we actually identified too many categories between held to maturity, available for sale, as one of the things that we felt needed short term work. Also, fair value and illiquid markets needed short term work. And so I would say our letter is consistent with your idea that we're going to do some short term work in these areas before we set out on really, really long term ideal scenario. That was the point we made in our letter, and I think our committee would probably still be supportive on that. With that, let me stop. That's kind of a thumbnail sketch of how our engagement has worked.

JM Just a report from our regulator, that's the Japanese regulator, the recent development to make Sir David happy, the kind of IFRS treatment in Japan, our advisory council called Business Accounting Council, has been discussing the possible application of the IFRS in Japan since last October 2008, and it has reached its interim conclusion as of January this year. And the gist of that report are just two points. The first one is the voluntary use or optional use of the IFRS could be permitted from the fiscal year ending 31st March of 2010 for the consolidated financial statement of the certain listed companies. That's the main idea. So it's not all listed companies, but it's major companies trading and international companies for the consolidated financial statements only. But certainly, we are thinking very seriously that it will start as of March 2010. So the statement will appear some time in mid 2010. So that's the first step of the voluntary use of the IFRS. The second one is the mandatory use of the IFRS. A decision could be made some time around 2012. Of course, this timing could be moved back and forth depending on the situations, other various factors of the development in Europe, the development in America, development everywhere; also that based on our own experience of the usage of the optional usage of the IFRS domestically. But those are the two major points of the report so that we are now moving forward to the adoption of the IFRS. Of course, that doesn't stop that there are efforts on the convergence which is targeted at 2011, as we agreed with each other. So that's one thing, but the other thing is that now that we are moving that way, not only the convergence but also the adoption of the IFRS, that's the paving the way for this direction. And then now that this draft is now under comment period, and comment period will be closed on 6th April, next Monday, so any of you would like to make comment do so in a hurry, please. Thank you.

GZ Thank you. Bob?

RG Chairman, the discussion has returned a couple of times to FAS 39. I just wanted to make a little further clarification surrounding David's comments on the proposal that the IASB taken to dealing with this, and that is a comprehensive overhaul over a period of six months. And I just make these clarifications because the members of the Monitoring Board were not party to our discussions this morning. David raised that, that proposal/plan from the IASB, within the context of a much broader discussion the Trustees had surrounding our commitment, as indeed I believe is the commitment of people in this room, to a single high quality standard which obviously would include FAS 39. It was, I think, the view of a large number of Trustees that such a standard doesn't come from a piecemeal set of changes that are done under pressure, that the way you get to that high quality standard is by treating the fundamental problem, not dealing with the symptoms. And that therefore the Trustees I think were very supportive of the approach that the IASB is taking to FAS 39. It's their view that this really is the way to get to the right solution to all of these problems, and indeed needs to be done quickly, and I think the proposal was to do it over six months. And it was indeed a quite broad discussion of that issue this morning.

GZ And it's good for you, Bob, that you remember... that you bring this up also in this meeting, because indeed this morning we had as Trustees quite extensive discussion on the issue. And there was broad enthusiasm not to stick to piecemeal changes but now to go to a real makeover of 39. That would be more productive than piecemeal repairs in a long run. Pedro?

PM Just a follow-up on that; I thank Mr. Maruyama for his information about the Japanese move to stage procedure, and I like very much that they are ready to remain involved in the convergence discussion. He made a previous point which I think is very much relevant to the discussion about our working group, or advisory group on the financial crisis. That's what the major, dramatic failure that we have was a failure of risk assessment models of many institutions and perceptions of risk on the part of regulators and supervisors. And it's one of the key reasons in addition to microeconomic ones that led to this crisis. So that's why, as we said in the morning prior to receiving members of the Monitoring Board, that since it is hard to imagine... let me give you an example to our American friends... it's very hard to imagine that what's going on now, stress testing with 19 large American financial institutions whose assets represents 88.5% of total assets of the 8,000 banks, it would, when it's ended, apparently by the end of next month, it should come out with some very interesting pieces of information for regulators, supervisors, and eventually standard setting on questions of capital adequacy, the pricing that would result from this public/private interaction in trying to get the balance sheet of banks to read of some distress or trouble with assets. There will be a lot of information there for regulators and supervisors and for us which should come out of this experience and the experience of some other countries trying to address similar problems. I'm leaving aside what regulators and supervisors will do, and surely they will have to do a lot of things in addressing the organisation in the US, the other types of organisations in Europe as well. But it will have some implications for us as well. I was happy to hear Mr. Hoogervorst mention that the advisory group has indicated that too much, perhaps far too much emotion went to the discussion about the differences between mark-to-market, mark-to-model, mark-to-hope, mark-to-muddle. The recent Geneva report came with a new suggestion. It said mark-to-funding that will complement the other categories involved. And this is a very interesting discussion, but the others have much less relevance, the question of the recognition or consolidation of balance sheets in which the presumption was that the risk had been shifted when in fact it had not been shifted entirely. So there's a lot of work to be done, and today in our morning conversation, we said, well, let's use this; let's not waste, let's not waste this opportunity for the lessons that we are deriving from the very discussion of why things went so badly wrong in trying to set up a new institutional setup in regulation, supervision and standard setting, and the interactions among them, because there are some types of interactions, to speed up the process. I think the readiness that Sir David indicated here to move quickly on the revision and simplification of IAS 39 in my view should be done together with FASB and together with the other regulators, the Monitoring Group. So we should use this opportunity to try to speed up the momentum for convergence. Everything I heard in the last several months since I've been here, especially in the last several months, have indicated that this is the right thing to do, and I don't think we should waste this opportunity.

GZ Mary?

MS Just very, very quickly, I agree with really everything you said, and we will use this opportunity and the sense of urgency on FAS 29 to try to get FASB to join hands with the IASB on a much accelerated timetable, if that's at all possible.

GZ Great news. Antonio? Thank you.

AV I'd like to go back to an issue of method versus content. And I want to pick on the difference of opinion that there was between you, Charlie, and David about... so David saying, well, the due process was leading to our active behaviour, and you saying, well, the European Commission was expecting a reply in a different timeframe. And I want to look at this and at the future with respect to the dilemma of accountability and independence. So we are accountable, we must be accountable, but independence is a part of our role. And if I go back and I look at the reality of this organisation, we have been setting international standards, global standards almost by ambition, but the reality is that Europe has been the privileged stakeholder. Europe in 2005 was the most keen in the game than anybody else. All the rest was a vision, had the vision to come and the IASB were global by... largely European by implementation, and this has determined certain expectations from the European Commission, from the Parliament, because the impact was fundamentally there. Now the game is changing, so we have countries like Japan, we have India, we have obviously the United States, we have other countries have already joined, but we are really moving from standards that are global by ambition to global standards by governments, I would say, by application. I wonder whether the European Commission, the European Parliament feel that... realise all this, and I am certain they realise, but if you feel very honest, that will entail a change of the expectation, a change of interaction. I'm really talking more about the Parliament versus you, Charlie. So it's going to be much more complex, the governments, the oversight, the interface with the truly global standard setter than it is for a standard setter applied only to Europe.

GZ Okay, Charlie. Can you give a short answer, because I want to close the official part of the meeting?

CM Well, I am pleased to note the earlier comment that there's going to be now a comprehensive review of IAS 39. Gerrit will remember this part of it in any event. When we were finance ministers in '04, and I finished on 29th September, we were assured from an earlier part that year that the IAS 39 discussion would be all over, and I was assured it would be all put to bed before I took over as Commissioner. So I'm delighted that five years later, that we're now going to get around to having a comprehensive review of it, so just to make the point. Secondly, I say to my friend here, he made a point that we were privileged to be first. Well, I don't think we were privileged because I think we have suffered from what I term ‘first mover disadvantage’ in this particular area, and so I will not be here this time next year, but I think that it will be good, and all the things I mentioned here today is that there's a fair degree of frustration built up in the European member states, there's a fair degree of frustration built up in the Commission. There's a lot built up in the European Parliament. And I think maybe what we've all been... what we should do, for those of us that believe in international standards, and someone like me who's always believed, long before I was in the privileged position of being the EU Commissioner in independance of standard setting for accounting, I remember the early '70s when we had things like international accounting standards they were called then. This is back in the '70s. Those were the beliefs at that time. I think it's in everybody's interests that stakeholders who have a big say in this are brought along, otherwise there's been a big move in Europe all the time, there are many member states, and a lot of influential people who would prefer to have one standard setter, okay, the European standard setter. And that I think should be borne in mind.

GZ Thank you very much, Charlie. I'll now try to close this meeting. I'm not going to try to summarise everything. I think one important issue we discussed today is that the IASB intends to do an overhaul of IAS 39, and we are extremely happy that the short track procedure also will be supported from the SEC and FASB. That is very good for the convergence process I think. This is one of the projects which could potentially make a lot of people happy. So thank you very much, and now I close the public part of the meeting. We have a few minutes still for the closed part of the meeting.