



# IAAER

INTERNATIONAL ASSOCIATION FOR ACCOUNTING EDUCATION & RESEARCH

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IFRS Strategy Review  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH

Dear Trustees of the IFRS Foundation:

In response to the IFRS Foundation Trustees' consultation paper, *Status of Trustees' Strategy Review*, we, the undersigned members of the Executive Committee (EC) of the International Association for Accounting Education & Research (IAAER) and the IAAER IFRS Consult Council (CC) are pleased to offer our comments on the IFRS Foundation's mission, governance, standard-setting process, and financing of the IFRS Foundation as requested in the Trustees' Strategy Review. The views expressed are those of the authors and do not necessarily reflect a consensus view of the IAAER membership, EC or CC. However, all members of both the EC and CC were requested to provide guidance that has informed our comment letter.

The mission of the IAAER is to promote excellence in accounting education and research on a worldwide basis and to maximize the contribution of accounting academics to the development and maintenance of high quality, globally recognized standards of accounting practice.

Our comments are supportive of the IASB's objective to develop one set of globally acceptable accounting standards, and are delivered with the intent to enhance the acceptability of IFRS worldwide.

**Mission: How should the organisation best define the public interest to which it is committed?**

1. The current Constitution states, "These standards [IFRSs] should require high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions." Should this objective be subject to revision?

*The objective as currently stated implies that external financial reporting is important to all who rely on external financial statements to make economic decisions with a primary objective of accounting standard setting being to meet the information needs of investors. Several of the EC and CC members that provided comments think, and we agree, that to be more consistent with*

*the IASB Framework “investors, other participants in the world’s capital markets” should be changed to “existing and potential investors, lenders and other creditors”. Responding members of the EC and CC vary in their views as to whether “other users of financial information” should be maintained in the constitution or dropped to be more in line with the IASB Framework.*

*In addition, given the IASB’s issuance of IFRS for SMEs, several members of the EC and CC believe the current objective does not adequately embrace the importance of IFRS for privately held companies.*

2. The financial crisis has raised questions among policymakers and other stakeholders regarding the interaction between financial reporting standards and other public policy concerns, particularly financial stability requirements. To what extent can and should the two perspectives be reconciled?

*The financial crisis has raised many questions about financial regulation from those reacting to the associated economic turmoil. However, we believe that standard setting should be proactive rather than reactive, and that any consideration given to the effects of accounting standards on financial stability should be based on hard objective evidence. Despite frequent assertions that accounting standards, particularly fair value standards, caused the financial crisis by overstating the extent of asset value declines, there is little academic evidence supporting this conjecture. After reviewing existing research, some members agree with The Report of the Financial Crisis Advisory Group that “it is unlikely that, on balance, accounting standards led to an understatement of the value of financial assets” that exacerbated the downward business cycle exhibited during the financial crisis.<sup>1</sup> Some members also agree with the SEC’s finding that those changes in fair values that were recognized were directionally consistent with the losses recognized on underlying loans that impacted the value of these securities.<sup>2</sup> This suggests that current accounting standards reflected economic conditions, not that accounting standards caused economic conditions, and causes some members to question why some continue seeking to fix the part of something that does not seem to be broken.*

*In fact, most contemporaneous research finds that accounting standards were more likely to overstate values than to understate them during the crisis. This has been attributed to the continued widespread use of historical cost accounting for financial instruments and impairment standards that allow firms to delay loss recognition. For example, Vyas examines the timeliness of write-downs taken by U.S. financial institutions during the 2008 financial crisis.<sup>3</sup> Results show that accounting loss recognition is less timely than fair value devaluations. Notably, the association between bank equity returns and implied but unrecognized losses suggests that indices used in fair value measures for items recognized at fair value provide a reliable indicator of loss even during periods of market illiquidity.*

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<sup>1</sup> Report of the Financial Crisis Advisory Group, July 28, 2009 available at <http://www.ifrs.org/NR/rdonlyres/2D2862CC-BEFC-4A1E-8DDC-F159B78C2AA6/0/FCAGReportJuly2009.pdf>.

<sup>2</sup> Office of the Chief Accountant Division of Corporation Finance, United States Securities and Exchange Commission *Report and Recommendations Pursuant to Section 133 of the Emergency Economic Stabilization Act of 2008: Study on Mark-to-Market Accounting*, December 2008.

<sup>3</sup> Vyas, D. 2011. “The Timeliness of Write-downs by U.S. Financial Institutions during the Financial Crisis of 2007-2008. Forthcoming *Journal of Accounting Research*.

*Beatty and Liao (2011) demonstrate the importance of timely loss recognition for healthy economic activity.<sup>4</sup> They find that delayed recognition of losses allowed under current GAAP for loans held for the production of income is associated with reduced lending. Specifically, relative to banks with more forward-looking loss provisioning, banks with less timely provisions reduce lending more during recessionary periods. This suggests that recognizing expected losses inherent in fair value estimates would not only provide a better representation of the asset value at the balance sheet date, but would be less procyclical than recognizing losses as they are actually incurred as called for by accounting standard “reformers”.*

*For this reason we do not believe that the IASB should, by fiat, change the objectives of financial reporting by subjecting accounting standards to a public policy review. Making financial stability or capital adequacy requirements an objective of IFRS would potentially diminish the usefulness of IFRS financial statements to other stakeholders who rely on them for their decision making. Rather, as the incoming Chair of the IASB, Hans Hoogervorst, noted in his speech in Brussels on 9 February 2011, accounting standards can make an important contribution to financial stability by providing guidance in generating transparent financial information. However, financial stability should be a consequence of increased transparency, rather than a primary goal of accounting standard-setters.*

### **Governance: how should the organisation best balance independence with accountability?**

3. The current governance of the IFRS Foundation is organised into three major tiers: the Monitoring Board, IFRS Foundation Trustees, and the IASB (and IFRS Foundation Secretariat). Does this three-tier structure remain appropriate?

*The governance structure has been modified following constitutional reviews in an effort to curtail criticisms that the composition of the IASB is biased in favor of specific geographical regions or practice backgrounds. However, several members of the EC and CC believe that the current geographic ‘targets’ in the Constitution have yielded perceptions that geographic representation has replaced technical expertise as “the” key criterion for Board selection and has accordingly given rise to concerns about the importance placed on technical expertise when selecting IASB members. In general, the EC and CC members that provided input for this letter support the IFRS Trustees’ continuing efforts to improve the identification of qualified IASB Board candidates from more diverse geographical and practice backgrounds to enhance the quality and independence of the Board; however, technical expertise should be a key criterion in the selection of every Board member.*

*In the last section of our letter, we highlight the importance of always having at least one member of the IASB with recent experience as an accounting academic. This latter issue was raised by many members of the EC and CC and was a reoccurring concern expressed at the IAAER World Congress in November 2010.*

*We also support the separation of the IASB Chair from the CEO of the Foundation, and the development of a more formal procedure and clearer criteria for the nomination and appointment of the Trustees.*

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<sup>4</sup> Beatty, A., and S. Liao, 2011. “Do Delays in Expected Loss Recognition Affect Banks’ Willingness to Lend?” Forthcoming *Journal of Accounting and Economics*.

4. Some stakeholders have raised concerns about the lack of formal political endorsement of the Monitoring Board arrangement and about continued insufficient public accountability associated with a private-sector Trustee body being the primary governance body. Are further steps required to bolster the legitimacy of the governance arrangements (including in the areas of representation of and linkages to public authorities)?

*Because public authorities generally have separate regulation rights over companies, requiring a formal political endorsement of the Monitoring Board appears duplicative and potentially over weights the reporting objectives of the regulators relative to other users.*

*Several members of the EC and CC providing input to this letter support the proposal to expand the membership of the Monitoring Board to include more capital markets authorities responsible for setting the form and content of financial reporting in their respective jurisdictions, with a focus on increased representation from major emerging markets, while limiting the overall size of the body to ensure efficiency and effectiveness.*

**Process: how should the organisation best ensure that its standards are high quality, meet the requirements of a well functioning capital market and are implemented consistently across the world?**

5. Is the standard-setting process currently in place structured in such a way to ensure the quality of the standards and appropriate priorities for the IASB work programme?

*The present process is widely respected because of the rigor involved and various efforts have been made to involve national standard setters on IASB projects. We suggest that the Board seek out more input from national standard setters during due process. Several members of the EC and CC highlighted the importance of having more preparers involved in the standard setting process to provide insights into, among other things, the cost and practicality of implementing proposed standards.*

*We encourage the IASB to focus on the quality of the standards as opposed to the quantity of the standards upon completion of the current work plan. For example, we applaud the June 2010 decision of the IASB and FASB to modify the targeted completion date for certain convergence projects by maintaining targeted completion dates of June 2011 or earlier for projects where the need for improvement is the most urgent with other projects being assigned a later completion date because they address areas that the IASB and FASB believe have a lower priority or where additional research and analysis is required. This modification represents an appropriate response to stakeholder concerns about their ability to provide quality input on the large number of major exposure drafts planned for publication in 2010.*

*We however note that the present agenda remains highly ambitious. Quality must not suffer due to the desire to meet what many view as unrealistic targets set by public authorities. We for example encourage the Trustees and Board to give serious notice to the statement made by PwC in July 2010 in response to the IASB and FASB decision to modify the MOU timetable.*

..... *Our experience with the standard setting process suggests that staff and Board members need sufficient time to thoughtfully consider constituent input; to analyze, evaluate, and consider alternatives; and to deliberate with other board members in order to issue standards that have duly considered all important ramifications and unintended consequences.*

*Recognizing the inherent need to balance speed to completion and efforts aimed at enhancing quality, we believe the targeted time periods in the Boards' recent release are not sufficient.*<sup>5</sup>

*Given the substantial number of new standards promulgated over the last several years, we also suggest the IASB increase its efforts in post-implementation reviews and that whenever feasible these reviews be completed before adding new projects to the work plan.*

6. Will the IASB need to pay greater attention to issues related to the consistent application and implementation issues as the standards are adopted and implemented on a global basis?

*To assess whether IASB standards are of high quality it is important to know how the standards are being adopted and implemented within and across countries. Current academic research provides evidence that IFRSs are being implemented differently by companies conditional on institutional and firm-specific reporting incentives (e.g., see Barth et al. 2010; Cascino and Gassen 2010; Lang et al. 2010; Liao et al. 2011).<sup>6</sup> These findings are not unlike those associated with other sets of financial reporting standards, as all accounting standards inherently allow discretion in accounting methods and estimates (e.g., U.S. GAAP). It is important to the mission of IFRS for the IFRS Foundation Trustees to increase their awareness of IFRS carve-outs, adaptations or implementation choices across countries.*

*We suggest that the IASB standard setting process include a phase of post-implementation review in order to gain knowledge on the adoption of its standards and identify best practices. Appointing an "Implementation Task Force" comprised of preparers, auditors, users, and academics (as noted below) might be beneficial to the reputation of the IFRS brand.*

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<sup>5</sup> PwC, *Point of View: Slowing down the pace of standard setting*, (July 8, 2010), available at <http://www.pwc.com/us/en/point-of-view/slowing-down-the-pace-of-standard-setting.jhtml>.

For an investor perspective, see also FASB Investors Technical Advisory Committee, Minutes of Meeting (July 13, 2010), available at

[http://www.fasb.org/cs/ContentServer?site=FASB&c=Document\\_C&pagename=FASB%2FDocument\\_C%2FDocumentPage&cid=1176158029190](http://www.fasb.org/cs/ContentServer?site=FASB&c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176158029190).

<sup>6</sup> See for example, Barth, M., W. Landsman, M. Lang and C. Williams. 2010. Are International Accounting Standards-Based and US GAAP-Based Accounting Amounts Comparable? Working paper, Rock Center for Corporate Governance; Cascino, S. and J. Gassen. 2010. Mandatory IFRS adoption and accounting comparability. Working paper, Humbolt University; Lang, M., M. Maffett, and C. Owens. 2010. Earnings Comovement and Accounting Comparability: The Effects of Mandatory IFRS Adoption. Working paper, University of North Carolina; Liao, Q., T. Sellhorn, and H. Skaife. 2011. The Cross-Country Comparability of IFRS Earnings and Book Values: Evidence from France and Germany. Working paper, University of Wisconsin-Madison.

**Financing: how should the organisation best ensure forms of financing that permit it to operate effectively and efficiently?**

7. Is there a way, possibly as part of a governance reform, to ensure more automaticity of financing?

*To date the IASB has been funded almost completely by voluntary contributions leading key constituents to voice concerns about the Board's independence. Members of the Monitoring Board are stressing the need for stable funding as the IFRS Foundation is reporting an 'unstable and unsustainable' budget position for 2011.<sup>7</sup>*

*Responding to concerns over its funding, post-2007 the Foundation's Trustees determined that funding should be broad-based, compelling (i.e. discourage free-riding), open-ended (i.e. without an automatic expiration date), and country specific (burden by country should be in line with GDP). We applaud this approach and encourage the Trustees to continue to focus on achieving this strategy.*

*In line with the Trustees present strategy, SEC Chair Schapiro has stated the goal is that funding of the IASB become mandatory in each jurisdiction. Funding should not be subject to 'We do not like this, so we will reduce our contribution'.<sup>8</sup> We agree and encourage the Trustees to redouble their efforts to achieve mandatory funding in all major markets based on GDP.*

**Other issues**

8. Are there any other issues that the Trustees should consider?

*We believe there are three other issues that the Trustees should consider as part of their strategic review.*

***Enhance the role of academics in the IASB standard setting process***

*First, we believe it is extremely important to enhance the role of academics in the IASB standard setting process. Academics are trained to be objective in their decision making; hence, their presence on the IASB serves to deflect political pressure inherent in the standard setting process. Academic involvement can be accomplished in multiple ways.*

*First, and foremost, it is important to have academic representation on the IASB. Having objective, independent Board members with rigorous thought processes is critical to the global acceptability of IFRS. Moreover, while the Board originally had academic participation, it currently is lacking in an academic member. Having an academic on the IASB is expected, both by academics and by others. The absence of an academic is viewed by many as a deficiency of*

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<sup>7</sup> S. Burckholder, SEC Wants Stable Funding for International Board As IASB Runs a Deficit, With Problems Forecast for 2011, The Bureau of National Affairs, Inc. (2010). See IFRS Foundation, Presentation of the Preliminary 2011 Budget, available at <http://www.ifrs.org/NR/rdonlyres/8E7190F7-6CED-436F-A719-38BC65AE2E8A/0/PresentationofthePreliminary2011Budget.pdf>.

<sup>8</sup> S. Burckholder, (2010).

*the Board's composition, particularly because other standard setters, notably the FASB, always have had academic Board members.*

*We remind the Trustees that in paragraph 10 the original Constitution (2002) stated “Three ... Trustees shall be selected after consultation with international organisations of preparers, users, and academics for the purpose of obtaining one Trustee from each of these backgrounds. Organisations consulted shall include ... and the International Association for Accounting Education and Research ...” Furthermore, paragraph 26 stated “To achieve a balance of perspectives and experience”, Board composition should include at least one academic. These statements were repeated in paragraphs 7 and 22 of the 2002 version of the constitution.*

*In 2005, the two statements were modified to be less specific. Paragraph 21 now states that “The Trustees shall select IASB members so that the IASB as a group provides an appropriate mix of recent practical experience among auditors, preparers, users and **academics**”. We note that the IASB presently includes members with recent experience as auditors, preparers and users but there is no representative with recent experience as an academic.*

*In terms of ‘recent practical experience’, perhaps some view an academic career in accounting as purely ‘conceptual’ or ‘theoretical’ in nature. True accounting academics normally have more training in accounting theory than do those pursuing other accounting and accounting-related career paths. Accounting academics however additionally possess expert-level knowledge in at least one area of accounting (e.g. financial reporting, auditing, taxation). To educate the next generation, accounting academics teaching for example financial reporting must possess up to date knowledge of the Framework, current financial reporting standards, and in many cases ongoing projects of the IASB. Indeed in comparison to most accounting and accounting - related professional backgrounds, academics are more likely than most to have a thorough, across the board knowledge of current IASB projects. Educating (teaching) others necessitates developing an extremely deep, comprehensive level of understanding of a topic.*

*In addition, because many accounting academics use financial reports as examples in our classes and in our research, we are well-versed in how accounting standards are implemented and interpreted. Hence, many of the accounting academics around the world that teach and research in the financial reporting area probably possess a more comprehensive level of expertise in financial reporting issues than those that have worked in a single company/firm their whole career.*

*Our view is that accounting academics do have experience that is directly relevant to what the IASB does; in other words, academics have recent practical experience.*

*As noted previously, at the IAAER 2010 World Congress, several participants voiced strong concerns regarding the absence of representation of our important constituency on the IASB. Our view – which is strongly supported by members of the EC and CC that informed our letter - is that the spirit of the constitution indicates there should at all times be at least one academic on the Board.*

*We encourage the Trustees to consider that academic representatives on the IASB can*

- *Help bring conceptually grounded, rigorous, and internally consistent thinking to Board discussions and decisions, while being open to considering a 'practical approach'. Thinking in a conceptual, rigorous way is stock and trade for academics but often does not come naturally to most non-academics.*
- *Help edit Board documents. Academics write for publication as a key part of their professional activity. The Board's output is the written word that needs to be clear and understood around the world.*
- *Infuse Board debates with knowledge gained from research - not just particular findings of particular papers, but a way of thinking about how we have learned that information is used and is useful in the capital markets.*
- *Help train new staff and new Board members to bring them up to speed on the status of the Board's projects. Also help develop existing staff. Academics are teachers and mentors. They naturally help educate and develop everyone they encounter.*
- *Provide a direct link to the academic community. This includes presentations and participation in various academic and non-academic conferences, and one-on-one discussions. Academics educate the accountants of the future. Having a direct link to those who are shaping the minds of the next generation is extremely important to promote the Board's thought processes and work. It also helps foster relevant research.*
- *Provide a sounding Board for staff ideas. Academics are used to discussing ideas, challenging ideas, and helping to develop ideas. This is what the staff is asked to do on its projects. Having a Board member who is experienced in this exercise is helpful to the staff.*
- *Assist in implementing the Trustees' Education Initiative activities. It is fitting for an academic to have a meaningful role in these efforts.*
- *Provide Board input into academic-related activities such as the KPMG IAAER Research Grant Program to inform the IASB and the EC of the IAAER.*

*In regard to the latter, we believe it is crucial that the position of Academic Advisor to the IASB be maintained at least until an academic is again assigned to serve on the IASB. In the absence of a direct link to the academic community, the IFRS organization runs the risk of distancing and disenfranchising one of its key constituents that is critical to the ultimate success of IFRS.*

*Second, the IFRS Foundation could appoint an IASB academic fellow(s) responsible for identifying and synthesizing academic literature relevant to standard setters as well as conducting more targeted studies to benefit the Board's deliberations. Third, the IFRS Foundation could host, perhaps in collaboration with the IAAER, an annual (or bi-annual) research conference where select studies would be presented to the Board. Finally, the IFRS Foundation could set up an academic council responsible for communicating contemporaneous research to the Board on a quarterly, semi-annual, or annual basis as well as engaging in field testing and evaluation of existing, proposed new standards or changes to standards. IAAER is willing to assist the Foundation in implementing these suggestions.*

### ***Provide guidance on XBRL tagging***

*We believe it is important for the IASB to address the need for specific XBRL guidance in promulgating new standards. Given an overarching objective of accounting standard setting is*



*to promote consistent and comparable financial information, it seems only logical to provide some guidance as to how financial data expected to be reported as a result of applying an IFRS be tagged in the IFRS XBRL system.*

### ***Translation of IFRS***

*Third, we suggest that the IFRS Foundation provide additional oversight over the translation of IFRS. When individual constituencies translate IFRS into their own relevant languages this increases the likelihood that mistranslations occur. At the same time, the IFRS Foundation does not have the resources to prepare the translations of IFRS to the universal set of languages. However, we encourage the IASB to continue considering the time, effort and consistency needed in effectively translating the English language version of IFRS into other languages. The existence of translation differences during the application of IFRS can threaten comparability (Doupnik and Riccio 2006; Tsakumis et al. 2009; Huerta et al. 2010).<sup>9</sup>*

*We thank you for giving us the opportunity to communicate our thoughts and suggestions to you.*

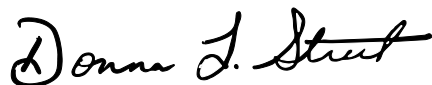
*Sincerely,*



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<sup>9</sup> Doupnik, T. S., and E. L. Riccio. 2006. The influence of conservatism and secrecy on the interpretation of verbal probability expressions in the Anglo and Latin cultural areas. *The International Journal of Accounting* 41 (3): 237-261. Tsakumis, G. T., D. R. Campbell, Sr., and T. S. Doupnik. 2009. IFRS: Beyond the Standards. *Journal of Accountancy* 207 (2): 34-39. Huerta, E., Y., Petrides and G. Braun. 2010. Lost in Translation: The Effect of Language on the Interpretation of IFRS. Working paper.

The following members of the IAAER Executive Committee endorse this letter:

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