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Mr Tsuguoki (Aki) Fujinuma &
Mr Robert Glauber
Vice-Chairs
IFRS Foundation
30 Cannon Street

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Düsseldorf, 24 February 2011

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Dear Mr Fujinuma,
dear Mr Glauber,

Re.: IFRS Foundation – Consultation Paper "Status of Trustees' Strategy Review"

We appreciate the opportunity to comment on the consultation paper mentioned above and would like to submit our comments as follows:

General Remarks

In its first decade, the IFRS Foundation has enjoyed significant success in establishing the International Financial Reporting Standards in a multitude of countries throughout the world. Both the importance attaching to, and application of, the IFRS are continuing to increase. The IDW therefore welcomes the fact that the IFRS Trustees have decided to review the organisation's strategy for the next decade.

In our view, continuing progress towards worldwide adoption of IFRS means that greater attention will need to be given to the governance of the institution, as well as its due process as a whole. Transparency and public accountability will constitute crucial factors in the future.

In this context, we are currently concerned that certain tendencies impair the quality of the IFRS and financial reporting according to IFRS, in particular:

- the increased complexity of the standards, which makes them difficult to understand, and may in turn lead to their incorrect application,
- inconsistencies between the IASB Framework and IFRSs as well as among the IFRSs,
- the pace at which new standards are issued and existing standards revised, and
- increasingly extensive disclosure requirements.

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

Question 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?

In our view, there is no need to change this objective. Financial statements prepared under IFRS are currently of most relevance to investors and capital providers. Therefore within the standard-setting process, the IASB has been focussing primarily on this group of users. One example of an investor-driven requirement is the measurement of all investments in equity instruments at fair value, despite the fact that in many jurisdictions the majority of investments in equity instruments do not have a quoted price in an active market, which means that this approach leads to increased measurement complexity, considerable additional costs, whilst reducing reliability.

In our view there are increasing demands for high quality financial information by other users as well, including employees, suppliers and prudential regulators. They also require relevant and reliable financial information in order to make their economic decisions.

In this context, providing information that both serves as a record of management’s accountability for past transactions and events and is capable of being reliably measured and verified is just as necessary as providing information of a more predictive nature to capital providers for use in making their respective investment decisions. Regrettably, management’s accountability has increasingly been given a back seat within the last years, despite the fact that ensuring reliability and verifiability of information presented in the financial statements is a significant factor in any consideration of the decision-usefulness of information. In our view, only by focussing on the provision of reliable and verifiable information will the IASB be able to ensure the acceptance of, and confidence in, the IFRSs by the divergent interested parties who, ultimately are those parties who support the sustainable development of the global economy.

The IDW is convinced of the need for the IFRSs to be global financial reporting standards that provide high quality, transparent and comparable information to users for making their respective economic decisions. However, the IFRSs have become increasingly complex, with disclosure requirements that are extremely voluminous and insufficiently clear and understandable. Although we acknowledge that such complexities are often due to today’s complex business environment and the increased complexity of many business transactions, we are concerned that financial reporting under IFRS runs the risk of its quality becoming increasingly impaired, which could also be detrimental to the acceptability of IFRS.

In order to ensure the quality and, in particular, the understandability and comparability of financial statements, we recommend that the IASB not merely increase the degree of detail of information to be provided within financial statements. Rather, the IASB should also try to identify a limited number of key indicators which could give users of financial statements a thorough overview of the reporting entities' financial position, performance and changes in financial position. Provided such indicators were precisely defined and standardised, they would be very helpful to users seeking to gain a first quick impression and also facilitate a comparison of several entities’ key figures, without the need to search through hundreds of pages of disclosure requirements.

Question 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?

Indeed, the financial crisis has raised questions among policymakers and other stakeholders regarding the interaction between financial reporting standards and other public policy concerns, particularly with regard to the stability of financial markets. Because of the increased importance attached to IFRS and the significance of their economic and legal impact on stakeholders, it is inevitable that the IFRS Foundation will face increasing political pressure in the future, seeking to influence the standard-setting process. However, financial reporting should only serve macro-economic objectives in so far as the provision of adequate information to stakeholders is concerned. Financial reporting should not become an instrument used to effect other regulations within the financial markets. For this reason, it is essential that the IFRS Foundation remains a private-sector body with a standard-setting body that retains complete responsibility for all technical matters pertinent to its agenda and that technical aspects remain based on an established Conceptual Framework for financial reporting.

Nevertheless, it will be necessary to discuss how legitimate political interests in respect of both the legal and the economic consequences of financial reporting ought to be considered. In our view, it might be helpful for political and other relevant stakeholders to be more involved in developing the Framework (we refer to our answer to question 5) as well as in the decision-making process concerning the determination of the IASB's agenda and priorities. Current consultation procedures, e.g. the three-yearly public consultation on the IASB's future technical agenda – as introduced in March 2010 following the review of the constitution – are not sufficient for this purpose. Increased involvement in the determination of the IASB work programme on the part of all major stakeholders would preclude the development of standards that are neither urgent nor necessary in the foreseeable future. Typical examples of such projects include "*Liabilities*" and "*Revenue Recognition*".

In addition, we would like to emphasise that the public consultation process should cover not only a discussion as to the potential items for the IASB's agenda, but also the objective, the scope and the priorities to be attached to those agenda items. We acknowledge that it will not always be possible to predict the entire development process of a project. However, it is important to determine the terms of reference for each project in order to avoid substantial decisions concerning scope and scale having to be made by the Board subsequently. Furthermore, the long-term work programme should be discussed with the IFRS Advisory Council prior to being finally approved by the Trustees.

In this context, we note that the comprehensive process for reaching decisions as to a re-exposure of proposals (e.g. in case of *"Amortised Cost and Impairment"*) is not formally regulated. To increase transparency, the IASB should explain the basis of its judgement underlying any decisions on whether significant changes to exposure drafts need to be re-exposed or not.

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

Question 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 IDW believes that the three-tier structure (Monitoring Board, IFRS Foundation Trustees and IASB) is appropriate for the governance of the IFRS Foundation.

Question 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?

We refer to our answer to question 2. Apart from this, we share neither the concerns of some stakeholders about a lack of formal political endorsement of the Monitoring Board arrangement, nor those about continued insufficient public accountability associated with a private-sector Trustee body being the primary governance body.

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?

Question 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 IASB has complete responsibility for the standard-setting process, including all technical matters and 'full discretion in developing and pursuing its technical agenda'. As mentioned above, the IDW believes that the IASB should take more account of stakeholders' input in developing or improving the IASB work programme (we refer to our answer to question 2). However, it is important that no single stakeholder group or geographical area dominate the IASB work programme and its priorities. All countries that have actually adopted the IFRS and thereby acquired practical experience should be able to exert influence.

In the more recent past, the IASB work programme has been overly influenced by the convergence project with the FASB. In general, we support both Boards' shared intention to reduce the differences between IFRS and US GAAP. However, the way in which the convergence project has been promoted does concern us. For example, as to the question of the most appropriate lessor accounting model, the IASB (staff) and leasing industry supported a sole derecognition approach that is consistent with the lessee accounting model and avoids double counting of assets. Nonetheless, the exposure draft contains the proposal of a hybrid model that appears, to us, to be an unsatisfactory compromise reached in order to achieve convergence with US GAAP "at any cost", since the FASB had rejected the derecognition approach. Therefore, we recommend the IASB bear in mind that convergence is not an end in itself, but should result in high quality global standards.

In general, the IDW welcomes the efforts made by the IASB to establish a standard-setting process that is as transparent and open as possible. Outreach activities, roundtable meetings, live webcasts, etc. are all steps in the right direction. However, we are concerned about the responsiveness of the IASB. Although respondents put a lot of effort and resources into writing comment letters or participating in IASB public conferences, the impression that many substantial comments have not been taken into account often remains when the final standards are issued. Serious concerns about a proposed standard made by a clear majority of significant commentators or a significant minority are rejected on the grounds that they have raised no new arguments and that these arguments have already been considered by the IASB during the development of the proposed standard. In our opinion, the Board should address such concerns once again and communicate any reassessment and its results publicly in order to ensure transparency and to achieve wide acceptance for the final decision.

Furthermore, the Framework should play a decisive role within the standard-setting process. It must form the conceptual basis for the IASB to draw upon in developing or amending standards. Moreover, from our point of view, the Framework should also provide fixed guidelines to which the IASB should pay greater attention. Currently, we are of the opinion that the significance of the Framework is not taken seriously enough, despite the fact that it could be an appropriate means to increase the accountability of the standard-setting process. For example, the involvement of all relevant stakeholder groups in developing the new Framework currently, the adherence to the final provisions as well as subsequent monitoring thereof by the Trustees, would improve the IASB's accountability and global acceptance of the IFRSs and would also reduce political pressure on the IASB's technical standard-setting process.

In relation to the development process of the new Framework, the IDW does not support dividing the project into several phases. Given the complexity of the diverse issues the phased approach adopted by the IASB will necessarily result in unintended consequences and lead to new inconsistencies.

The publication of an exposure draft or an IFRS currently requires approval by nine members of the IASB, if there are fewer than sixteen members, or ten when there are sixteen members. Given the increasing significance and use of the IFRS worldwide, in order to enhance the acceptance and technical quality of IFRS, it is essential to have adequate support within the Board for the publication of an exposure draft or an IFRS. Issues that are especially controversial in nature should be carefully considered and based on wide support within the IASB before being published. Therefore, we would appreciate the IFRS Foundation requiring a sufficiently large majority vote to approve the issuance of exposure drafts and standards. This means that a larger majority should be required for voting on exposure drafts or for finalising IFRSs. At present, we suggest increasing the majority to 10, or 11 when the number of Board members is increased to 16, respectively.

Question 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?

The IDW believes that as the standards are increasingly being adopted and implemented on a global basis, there is a need for greater attention to issues related to their consistent application and to address implementation issues that may arise. Therefore, we welcome the Board's decision to conduct a post-implementation review of revised standards two years after they became effective (e.g. IFRS 3 and IAS 27). However, this does not mean that the IASB should play a role in the enforcement of IFRSs.

In our view, the propensity for consistent application is inevitably linked to the quality of the underlying reporting standards. In this context we would like to emphasise the need for principles-based standards as these have the advantage of facilitating application in a variety of situations and circumstances and, at the same time, preclude the need for undue regulatory intervention in the form of detailed rules that would then be applicable in every conceivable situation. Although, we consider it important that the standards are, as far as possible, sensitive to the legal impediments and economical particularities of the jurisdictions in which they are to be applied, efforts to attain convergence at any cost give rise to the risk that the standards will continue to become more and more rules-based (we refer to influences of FASB regarding “*Revenue Recognition*” and “*Leases*”).

The increased complexity, the pace of change and the increasingly extensive disclosure requirements also impair the quality of the standards. There is a danger that the multitude of complex requirements (e.g. the increased use of expected values) may not be fully understood and applied in practice; both of which may lead to incorrect and thus inconsistent application. The same is true of the current pace of change in the development of new standards, which, in our view, should not continue. Each standard needs to be sufficiently robust so as to remain valid for an extended period. In this context, neither the costs of changes should be underestimated, nor the practicalities of application.

Considering the multitude of recently finished projects and the ongoing projects (e.g. replacement of IAS 39 and leases) and the resulting implementation challenges afterwards, we would like to suggest the Board envisage a “period of calm” for the whole development process – not only the publishing – of new standards post 2011. During this period, the IASB could complete the outstanding “post-implementation review” and remedy deficiencies within the current standards (i.e. annual improvements). Additionally, there would be the time to finalise the Conceptual Framework Project in order to provide a valid and consistent basis for developing future standards, which, from our point of view, is absolutely essential (we refer to question 5). Moreover, a “period of calm” would bring a period of real respite for all users and preparers of financial statements who are currently occupied with understanding and implementing the amendments and new standards recently published as well as the standards and amendments that are due to be published by mid 2011.

Another important challenge the Board could address within such a period is the comprehensive review of the current disclosure requirements in the IFRSs. In our view, there is a need to consider each of the disclosure requirements in terms of necessity because currently, as we have commented on several occasions, it appears to us that the Board often proposes new disclosures almost as a matter of routine, even though only a single group of users has expressed a desire to receive a particular piece of information. The resulting information overload makes the financial statements increasingly confusing. For preparers, the increased volume of disclosure requirements leads to the routine ticking off of checklists, uncertainty concerning material information and undue costs surrounding the capture and preparation of the required information. For users, it also becomes more and more difficult to determine which information is really useful in decision-making.

For these reasons, in addition to the consideration of key indicators (referring to question 1), we would like to recommend the IASB undertake a comprehensive review of the current disclosure requirements. We are convinced that leaving out some of the detailed information and focusing instead only on essential information could result in more meaningful reporting. It could be helpful to develop a “Disclosure Framework” providing principles and fixed guidelines for disclosure requirements. In this context, we also refer to the IAASB Discussion Paper: The Evolving Nature of Financial Reporting: Disclosure and Its Audit Implications. The IPSASB is also currently in the process of considering this as the final part of its own Conceptual Framework Project. With respect to the issues that a Conceptual Framework ought to cover beyond disclosure, we would also like to refer to the IDW Concept Paper from 2007 “Additional Issues in Relation to a Conceptual Framework for Financial Reporting”.

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

Question 7:

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

We continue to support the efforts of the Trustees towards the establishment of a broad based funding system to help ensure the sustainability of the standard-setting process. Furthermore, the IDW welcomes the European Union’s stated intention to extend their contribution to the funding of the IFRS Foundation, which would reduce the necessity for private funding.

Other issues

Question 8:

Are there any other issues that the Trustees should consider?

We are not currently aware of any further issues that need to be considered by the Trustees.

We would be pleased to answer any questions that you may have or discuss any aspect of this letter.

Yours sincerely

Klaus-Peter Naumann
Chief Executive Officer

Norbert Breker
Technical Director
Accounting and Auditing