By E-mail: strategyreview-comm@ifrs.org

International Financial Reporting Standards Foundation
30 Cannon Street
London
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24 February 2011

Dear Sirs

**IFRS Foundation Trustees' Review of Strategy**

We appreciate the opportunity to respond to this important consultation issued by the IFRS Foundation Trustees in connection with their review of the strategy of the organisation.

This response summarises the views of member firms of the PricewaterhouseCoopers network that commented on the consultation. "PricewaterhouseCoopers" refers to the member firms of PricewaterhouseCoopers International Limited, each of which is a separate legal entity.

Our views on the specific questions raised by the Trustees are included in the accompanying Annex. In this covering letter we provide some overall observations on what we consider to be important issues connected with this review.

**Scope of Trustees' and Monitoring Board reviews**

We note that the Trustees are undertaking this review of strategy at the same time as the Monitoring Board of regulatory authorities is reviewing the governance of international accounting standard setting. There is a clear linkage between the two reviews, and some significant overlap in content, notably in the area of governance.

The parallel but different review processes being operated by the Trustees and the Monitoring Board have resulted in some confusion for stakeholders. We are pleased to note the recent announcements indicating that there will be enhanced coordination of the two reviews, and hope that subsequent consultation steps by the respective bodies are taken simultaneously so that the combined impact of the proposals can be evaluated by stakeholders.

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We will respond to the Monitoring Board's consultative report in due course. In the meantime, our responses to the Trustees' questions on governance in this letter are relatively brief. We will provide more detailed views on governance to the Monitoring Board, since we understand its review focuses on those aspects, while the Trustees' review is now anticipated to be oriented around the due process and operational aspects of the organisation.

**IFRS implementation activities and scale of operations**

In addition to the related Monitoring Board consultation, we note that the Trustees are also undertaking separate reviews of the effectiveness of the IFRS Interpretations Committee and of the structure and operations of the IFRS Advisory Council.

We believe these various reviews are inter-linked. As indicated in our response to Question 6 we observe that there seems to be an expectation gap in the marketplace regarding the volume of interpretation and application guidance that the IFRS Foundation provides.

At the same time, as a result of the volume of major new standards to be released in the next year and the fact that more market economies are currently adopting or making the transition to IFRS, we can see the demand for Interpretations and Improvements of IFRSs increasing further. The Strategy Review provides the Trustees with a valuable opportunity to consider whether all aspects of the current operational structure are sufficiently scalable to address the ever-increasing stakeholder base as more countries around the world transition to IFRS.

We therefore urge the Trustees to study carefully relevant stakeholders' input on these matters in the context of the review of the Interpretations Committee, as well as the direct responses to this Strategy Review.

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We would be delighted to discuss our views further with you. If you have any questions in the meantime regarding this letter, please contact John Hitchins (+44 207 804 2497), Ian Dilks (+44 207 212 4658) or Graham Gilmour (+44 207 804 2297).

Yours sincerely

PricewaterhouseCoopers LLP

**ANNEX**

# Detailed responses to questions in the consultation paper 'Status of Trustees' Strategy Review'

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

**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 be subject to revision?**

No. We do not believe that the mission as currently stated in the Constitution requires revision. We consider the primary objective of financial reporting (and hence of financial accounting standard setting) is to report to investors and others in the capital markets so that they can make economic decisions. It is in the public interest to have well-functioning and orderly capital markets and to have a comprehensive set of financial accounting standards that help underpin those markets. Those standards should enable investors and others to understand the economic performance, cash flows and economic risks displayed by companies.

The financial crisis has, as Question 2 indicates, raised questions regarding the interface between financial reporting and financial stability. As an important element of well-ordered capital markets, financial accounting standards already make a direct contribution to financial stability. Transparency, including a proper appreciation of risk emanating from the business model, is essential to the sound and effective operation of capital markets and to financial stability. We believe that, to the extent that financial accounting standards might have financial stability implications, these should be addressed as part of the deliberative process in developing the standards. This is discussed further in our response to Question 2.

We do not consider that the remit of the IASB should be expanded to other areas (eg public sector and not-for-profit) at present, since the Board already has a very full agenda in dealing with financial reporting for the capital markets.

**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?**

Whilst financial stability may not, as noted above, be the primary role of financial reporting and financial accounting, it is an important consideration. We encourage the IASB to continue to work closely with the regulatory community (for example through its regular "enhanced technical dialogue" with a range of regulatory organisations). The IASB should also include as part of its due process (and reflected in the Due Process Handbook) a step that, where it believes its proposals may have financial stability implications, it ensures that regulators are included in the consultative process. This should be a two-way exchange, such that regulators are informed of the Board's thinking and, at the same time, the Board is aware of regulatory considerations. Regulators and the Board would have the opportunity to think through any implications or unintended consequences of proposed changes to accounting standards, and any actions that they each might need to take to pursue their respective objectives.

An example of the interaction between financial reporting standards and financial stability requirements is in providing for impairment of financial assets. The IASB, in its Financial Instruments project, is moving from a model of recognising incurred losses to recognising expected losses on loans currently held, consistent with the principles in the Conceptual Framework and following feedback from users that this would give greater transparency. Prudential regulators, by contrast, are interested in exploring provisioning mechanisms for regulatory capital purposes in order to smooth losses over the whole economic cycle (ie, including on loans not yet held), increasing individual banks' ability to absorb future losses.

In our view, investors are interested in making economic decisions based on the risks inherent in the assets and liabilities currently held by the entity, while regulators have different mechanisms that are open to them in order to pursue prudential objectives. In this situation the differing objectives of the two approaches potentially conflict, but in practice can both be met by using different tools: accounting standards on the one hand for investors; and capital requirements, for regulatory purposes, on the other. Therefore, where there is a conflict, which we would expect to be infrequent, between financial reporting and prudential or other public policy objectives, we would expect regulators to consider tools other than accounting standards in order to achieve that objective.

## <u>Governance: How should the organisation best balance independence with accountability?</u>

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

Yes. Although we would not regard the IASB itself as part of the *governance* structure, we believe the current three-tier model remains appropriate. We note also that the consultative report published by the Monitoring Board envisages retention of the three-tier structure.

We have observed occasions when the current structure has seemed to lack clarity and simplicity (evidenced by the initial lack of clarity and coordination regarding the separate and overlapping reviews being undertaken by the Trustees and the Monitoring Board) and we have considered other possible models – for example whether elements of the present

Trustees and Monitoring Board could be combined into a single body. However we do not believe that such an alternative structure would result in greater simplicity or effectiveness.

We believe the Monitoring Board provides a valuable and suitable setting for capital markets regulators to meet and discuss views on the direction of financial reporting and standard setting. The regulators do have an important and unique perspective and should have the opportunity, via the Trustees, to express views to the IASB on the direction of accounting standards. We also consider it important that the Monitoring Board should continue to include members that are sufficiently senior in their organisations to represent those organisations' points of view with authority.

The day-to-day work of holding the IASB to account for its operations and due process should remain with the Trustees, with the Monitoring Board holding the Trustees accountable for ensuring that the IASB follows due process. We also believe it would help reinforce the role and accountability of the Trustees if they could be more visible in explaining their role and activities, and by enhancing communications about those activities - for example by having a separate section of the IFRS Foundation website that highlights the work of the Trustees.

Hence, while we believe the current basic three-tier structure (IASB + Trustees +Monitoring Board) should continue, the Monitoring Board's roles and responsibilities vis a vis those of the Trustees should be set out with greater clarity. We consider that enhanced clarity of roles should be a primary objective of the respective reviews currently being undertaken.

**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 will comment in detail on these matters in our response to the Monitoring Board's consultative report (including on issues such as the extent to which the Monitoring Board should be involved in the selection of Trustees and IASB members and the extent of the Monitoring Board's powers with regard to the work agenda of the IASB).

**<u>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?</u>**

**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?**

Please refer to our comments in relation to Question 3 above regarding the extent of the Monitoring Board's powers and the Trustees' responsibility to hold the IASB to account for due process.

We note that the IASB has already committed to consulting publicly on its work programme on a periodic basis, beginning this year. This was a key area of stakeholder comment during the last Constitutional Review and we welcome the willingness of the Trustees and the IASB to introduce this measure. The IFRS Advisory Council has already had a number of opportunities to input to the post-2011 work programme.

A key finding from the Advisory Council's discussions was that the quality of the standards would be reinforced if the Board's project on the Conceptual Framework was completed on a timely basis. Consistency with a clear conceptual framework was one of the characteristics for writing good standards cited in the paper *'Principles-Based Accounting Standards'* (January 2008) issued by the Global Public Policy Committee of the six largest audit networks. We have previously provided a copy of this paper to the IASB and would be pleased to have a further opportunity to discuss its contents.

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

Yes. In our response to the Trustees on the review of the IFRS Interpretations Committee (dated 31 January 2011) we observed that there seems to be an expectation gap in the marketplace regarding the volume of interpretation and application guidance that the IASB and the Interpretations Committee provide. Stakeholders seem to believe that more interpretation and application material is needed than is currently provided by the Board. We also noted that some members of the IFRS Advisory Council have commented in meetings that they would like to see the IASB involved more closely in matters related to the consistent application and implementation of the standards.

While we agree that IASB does not have enforcement responsibilities, we consider that there are a number of steps the Board could take that would help towards the goals of consistent interpretation and implementation: it should seek to collect information on instances where there is known to be inconsistent application; it could obtain input from national standard setters on implementation practices; and it could conduct post-implementation reviews of the standards with a particular focus on application aspects.

Further, we consider there would be benefit in having an international forum whereby regulators, the IASB and others can compare notes and discuss matters of application and implementation (this already occurs to some degree, for example in Europe through the European Securities and Markets Authority, formerly CESR). Where local interpretations appear to conflict with IFRS, there may be a role for the IFRS Interpretations Committee in resolving such situations.

The Board has been under significant pressure to complete its current programme of work, in particular the Memorandum of Understanding (MoU) projects, by the middle of 2011. Inevitably, there may be some elements of the new standards that, with the benefit of experience, might be improved or clarified. As a result, we can see the demand for Interpretations and Improvements increasing further in the next few years. In addition, as more major market economies transition to or adopt IFRS in the coming years, this may also stimulate the demand for interpretations and application guidance.

Therefore, we believe the Trustees should evaluate whether various aspects of the Foundation's operations, including Interpretations Committee and other Implementation activities, are sufficiently scalable to address the organisation's ever-increasing stakeholder base and expectations.

The Trustees recently announced the Foundation's intention to open an Asia-Oceania liaison office in Tokyo. As the demands from stakeholders on both the technical and other resources of the Foundation increase over the coming years, matters that might be considered include:

- The role of branch or liaison offices;
- The extent to which the IASB can partner with or share work with national standard setters, either individually, or in groupings; and
- The means by which regional and/or functional groups of stakeholders can be developed to assist with outreach.

We appreciate that the Foundation is currently working within a tight monetary budget and the organisation is not presently staffed and resourced to a level that would facilitate more intensive monitoring by the Board of the adoption and application of its standards around the world and greater involvement in implementation matters. However we believe it is better to consider what, ideally, the Board should be doing, and then assess whether the resources are available to match those objectives.

**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?**

We believe that a stable funding mechanism will only be achieved if a levy-based system is devised – with amounts to be raised in specific territories allocated by reference to some appropriate criteria (for example: share of global GDP; share of world market capitalisation; by G20 membership, etc). A number of principles could be devised to guide the design of the funding regime – for example the system should be transparent; build in inflationary rises; be independent of the political process; and be free from perceived conflicts of interest.

In our view the Monitoring Board could play a valuable role in helping to facilitate a stable funding mechanism.

## Other issues

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

We have no further comments to add at this stage.