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Trustees of the IFRS Foundation
30 Cannon Street
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Dear Trustees

Paper for Public Consultation - Status of the Trustees' Strategy Review

The global organisation of Ernst & Young is pleased to respond to the Paper for Public Consultation – Status of the Trustees' Strategy Review.

We fully support the Trustees' decision to consult stakeholders in their efforts to enhance the IFRS Foundation's strategy and provide transparency into the strategy development process. Addressing the key concerns surrounding the IFRS Foundation's mission, governance, processes and financing is crucial to achieving the overall goal of a high quality global set of standards. Our detailed responses to specific questions in the paper for public consultation are set out in the Appendix to this letter.

Mission

We recognise that defining the public interest is of paramount concern in developing standards that are not just high quality, but also based on consistent principles. In our view, the definition of public interest needs to be closely aligned with the objectives of financial reporting resulting in the public interest being best defined as 'existing and potential investors, lenders and other creditors'. Whilst the needs of other financial statements users are often aligned with the needs of these 'primary' users, we recognise that there may be areas of divergence. In our view, any gaps would be best served with increased transparency and supplementary disclosures. Ultimately the needs of the primary users must be considered above all others, as these are the users who would lack the ability or power to obtain the information they need from the reporting entities through other means. Aligning the public interest that is served by the IFRS Foundation with the primary users will create greater clarity in the IFRS Foundation's decision making process and in the development of standards for use by that public interest group.

Governance

Overall, we are supportive of the existing three tier structure of the IFRS Foundation as a means towards incorporating independence into the standard setting process. The role of the Monitoring Board should continue to be limited to an oversight role with no involvement in or influence over the content of the IASB's agenda or the agenda setting process. In addition, we believe there should be greater clarity on the roles and responsibilities of these three distinct groups. This includes providing more transparency into the activities performed by these groups (in particular the Trustees).

Process

Consistent application of standards by the global community is a requirement of having a truly global set of standards. We believe that expanding the role of the IFRS Interpretations Committee to issue short interpretations within a limited time frame will be a significant step towards achieving this goal. We also believe that the Monitoring Board can assist in this area by discouraging divergent views or interpretations by individual countries and regulatory bodies.

Financing

The Trustees and Monitoring Board need to demonstrate that the standard-setting process is sufficiently independent and robust so that all stakeholders accept IFRS, as issued by the IASB. The best method for achieving this goal is to establish a transparent and non-voluntary funding mechanism overseen by the Monitoring Board and tied to those capital markets that utilise IFRS.

Should you wish to discuss the contents of this letter with us, please contact Ruth Picker or Leo van der Tas on +44 (0) 20 7951 3152.

Yours faithfully

Ernst & Young

Appendix – Responses to the questions in the Paper for Public Consultation: Status of the Trustees' Strategy Review

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?**

In our view, the Trustees should amend this objective to align the definition of the "public interest" in the constitution with the objective of financial reporting. The *Conceptual Framework for Financial Reporting 2010* identifies that the objective of financial reporting is to meet the needs of 'existing and potential investors, lenders and other creditors'. We believe that investors, lenders and other creditors should be the primary users of financial information, with other stakeholders' needs viewed as secondary.

We are concerned that defining the public interest too broadly will lead to conflicting needs. This could result in inconsistency in standards and consequently result in lower quality standards, which is contrary to the goal of establishing high-quality global standards.

Also, in our view *public interest* is related to the objectives of financial reporting which is ultimately dependent on how the users of financial statements are defined; whereas enhancing the IFRS Foundation's *public accountability* to its stakeholders should be predominantly addressed through the structure, membership and overall governance of the Monitoring Board.

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?**

Some would argue that the role of financial reporting standards may conflict with other public policy concerns, such as financial stability requirements. An often cited example of such a conflict would be in a period of market volatility, where financial stability concerns would appear to call for smoothing of profits from period to period; however transparency would require presenting the reality that profits are not in fact smooth. In our view, a lack of transparency under the guise of financial stability would only create a temporary form of stability. Once revealed, this lack of transparency would decrease user confidence in the capital markets, which is contrary to the long term view of financial stability.

Accordingly, we believe these two perspectives are not irreconcilable, nor inherently conflicting. In the end transparency benefits not just the investor but also those concerned with financial stability. A good example of when these objectives have proven to be converged can be seen in the proposed treatment for expected loss provisioning, where the standards are striving to meet the needs of financial statement users, whilst also aligning substantially with financial stability concerns. However, we believe that attempts to reconcile these views when there is perceived divergence would be difficult to achieve while still maintaining high quality standards that are developed based on consistent principles.

In forming our view we have considered whether financial statements prepared under IFRS are meant for 'general purpose' or 'specific purpose' and how this concept is related to the capital markets. The *Conceptual Framework for Financial Reporting 2010* highlights that '*many existing and potential investors, lenders and other creditors cannot require reporting entities to provide information directly to them and must rely on general purpose financial reports for much of the financial information they need.*' Following this concept results in financial statements prepared with the needs of these primary users in mind, as they are the users that lack the power and ability to independently obtain information from these entities. It is this that drives the need for financial reporting standards to ensure fairness and transparency of information. Accordingly, financial reporting standards should consider the needs of those primary users who are unable to obtain information through other means above the needs of all other users.

With this concept in mind, we believe that although the needs of the prudential regulators are generally aligned with the requirements of financial reporting standards, any remaining gap should be bridged through additional disclosures and enhanced transparency of financial reporting. If there are requirements to meet other specific users' objectives and requirements that diverge from the general purpose and objectives of financial reporting, prudential regulators have the power and ability to require the information they need through other methods separate from general purpose financial reporting.

We are concerned that should the specific needs of prudential regulators be taken into account in external financial reporting standards, it could be argued that other broader interest groups should have their specific needs addressed by financial statements as well. For this reason, we believe the public interest should be confined to the objectives of financial reporting noted in Question 1 above.

We also believe that financial reporting is important in the efficient functioning of capital markets and capital flows and recognise that certain standards will impact an entity's behaviour and aid in forming the users' overall view of an entity (for example, environmental obligations presented as liabilities will influence users' perceptions of what is a present obligation of that entity; related party disclosure requirements may discourage an entity from entering into such transactions). In our view, the concern for standards setters is not to ensure neutrality of standards, but instead to ensure a lack of bias in the development of standards. The focus should be on how best to take into account these potential consequences in the development of financial reporting standards focusing on the primary users' needs, with all other stakeholders' concerns viewed as secondary.

Appendix – Responses to the questions in the Paper for Public Consultation: Status of the Trustees' Strategy Review

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?

We do not believe that there is necessarily a conflict between independence and public accountability and, as a matter of process, independence and the freedom and opportunities this creates increases the need for accountability. The independence of an organisation from the public interest it serves would provide more reason to be accountable and communicate what that organisation has done with this responsibility and to legitimise the organisation and its actions. Instead the potential conflict would be seen between independence and the public interest and ensuring there is no perceived or real dependency on any particular public interest group.

We are supportive of the three-tier structure; however believe that the distinction and roles of the Monitoring Board and the IFRS Foundation Trustees should be clarified.

The role of the IASB is to set global standards and, accordingly, the IASB is not accountable to a single jurisdiction (government, securities regulator). In our view, the role of the Monitoring Board is to create a link between the IASB and public authorities that would not otherwise exist in a global standard setting process. As a result, we believe it is imperative that the Monitoring Board have oversight of the standard setting process with no direct involvement in agenda-setting or technical decisions to maintain this accountability role. The Trustees' role is important in the standard setting process to ensure continued involvement of the private sector and the profession.

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 believe that the organisation should address concerns surrounding the transparency of the Trustees to enhance legitimacy. The Trustees have been selected as influential and respected members within the global business community who should be seen more frequently by the public. This would allow stakeholders to have greater visibility into the work the Trustees perform and the support they provide to the IASB. The Trustees should also provide greater transparency into the governance process (such as the appointment process). Enhancing transparency and visibility would provide stakeholders with greater understanding of the Trustees' role and processes to achieve more confidence from stakeholders.

Appendix – Responses to the questions in the Paper for Public Consultation: Status of the Trustees' Strategy Review

We have not provided our views regarding the structure, form and governance of the Monitoring Board as we understand a separate consultation process regarding the role and governance of the Monitoring Board is in progress.

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?**

We believe that the current structure and processes in place, as set out in the IASB Due Process Handbook, contribute to ensuring high quality standards. We commend the Board for the degree of outreach that has occurred recently and encourage continued field testing as integral to the process of developing high quality standards. In our view, the structure could be enhanced by expanding and clearly defining the role of the IFRS Interpretations Committee (Interpretations Committee) as noted in our response to Question 6.

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?**

We agree that consistent application and implementation issues should be an area of focus in ensuring a high quality global standard is achieved and this is a key role that could be fulfilled by the Interpretations Committee. As we stated in our comment letter on *The Annual Improvements Process: Proposals to amend the Due Process Handbook for the IASB*, we believe the Interpretations Committee should be able to issue interpretations (rather than agenda decisions) within a limited timeframe. Allowing timely response to constituents' application and implementation concerns is paramount to maintaining high quality global standards. Further, this will allow the IASB to continue its focus on significant issues and maintaining high quality of the standards themselves.

We also believe that the Monitoring Board can play an important role in this process by discouraging differences within the markets and deterring regulators from issuing independent implementation rules.

Appendix – Responses to the questions in the Paper for Public Consultation: Status of the Trustees' Strategy Review

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 agree that financing is a key issue. In our view, the IFRS Foundation needs to establish a long-term sustainable process that spreads its sources of financing out and establishes a non-voluntary funding process. This would allow the IFRS Foundation to avoid the appearance of influence. The appropriate source of funding should be tied to the definition of public interest established by the Trustees in response to Questions 1 and 2 above. We also believe funding should be the responsibility of the Monitoring Board and not of the Trustees which aligns to the roles set out in our response to Question 3 above.

In summary, we believe the IFRS Foundation needs to establish a transparent and non-voluntary funding mechanism that is tied to the definition of public interest and overseen by the Monitoring Board. The source of automatic funding should be clearly linked to the capital markets that are supported and utilise IFRS.

Other issues

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

We have no further comments to make.