IFRS Foundation
30 Cannon Street
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Re.: Trustees' Strategy Review

I appreciate the opportunity to comment on the paper published by the IFRS Foundation Trustees in the context of their comprehensive review of the Foundation's strategy in November 2010[1].

I am a resident scholar at Bruegel, a European think tank which started operations in Brussels in 2005, and a visiting scholar at the Peterson Institute for International Economics, based in Washington DC. I am also a member of the CFA Institute's Corporate Disclosure Policy Council, of the International Corporate Governance Network's Accounting and Auditing Practices Committee, and of the French Accounting Standards Authority's Advisory Council. This letter represents my personal views and not those of any of the above mentioned organizations. Accounting standard-setting is a topic on which I have conducted research almost continuously in the past decade, first in France and then in an international context[2]. I believe that my work commitments and activities do not introduce any commercial or special-interest bias to my views nor do they impair the integrity of my research[3].

This letter follows comments I had contributed in both phases of the Foundation's latest Constitution Review[4], as well as a response to the US Securities and Exchange Commission's consultation on its proposed "roadmap" in 2009[5]. As I intend to also contribute to the forthcoming next phase of the Strategy Review with a paper based on more in-depth research, this letter is kept relatively short and narrowly focused on the questions asked in the November document.

As one of those who opined that the last Constitution Review had stopped short of the governance changes that would be needed to put the IFRS Foundation on a sustainable path, I can only applaud the initiative to launch this Strategy Review. The fact that there is now a parallel consultation process from

[1] IFRS Foundation, "Status of Trustees' Strategy Review", Paper for Public Consultation, 5 November 2010, available on www.ifrs.org

[2] See in particular "La Mondialisation en partie double : La Bataille des normes comptables" (with Philippe Crouzet), En Temps Réel, Paris, March 2002 ; *L'Information financière en crise – Comptabilité et capitalisme* (with Matthieu Autret and Alfred Galichon), Odile Jacob, Paris, May 2004; *Smoke & Mirrors, Inc.: Accounting for Capitalism* (with Matthieu Autret and Alfred Galichon), Cornell University Press, July 2006; and *The Global Accounting Experiment*, Bruegel Blueprint Series, April 2007

[3] A comprehensive list of these commitments and activities is available on www.bruegel.org

[4] Published by Bruegel, respectively, as "Empower Users of Financial Information as the IASC Foundation's Stakeholders", Bruegel Policy Contribution, July 2008; and "IFRS Sustainability Requires Further Governance Reform", Bruegel Policy Contribution 2009/14, December 2009, both available on www.bruegel.org

[5] Published by Bruegel as "A US Strategy for IFRS Adoption", Bruegel Policy Contribution 2009/06, April 2009, available on www.bruegel.org

the Foundation's own Monitoring Board[6], which has been criticized by some respondents, should not come as a surprise given the autonomy of the Monitoring Board from the Foundation's Constitution framework (see my response to question 3 below). Even as these consultations take place in a politically constrained context, they hold the potential of delivering improvements in the Foundation's governance arrangements, and ultimately in the quality of IFRS standard-setting and of financial reporting practice around the world.

In the text below, the sections in italics reproduce the questions listed in the Trustees' paper.

Mission

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?

This wording is too ambiguous as to which stakeholders' needs IFRS standard-setting should serve in priority. This ambiguity may have been beneficial to IFRS standard-setting in the past, but no longer is in the present circumstances. The Foundation should more clearly state that its priority stakeholders are investors, as it cannot respond equally to all information needs of all users of financial information without seriously compromising the quality of its standards.

Both the IASB's conceptual framework and the Monitoring Board's landmark statement on principles in September 2009[7] are more precise from this standpoint. The Monitoring Board's statement refers to "the primary objective of financial reporting as being to provide information on an entity's financial performance in a way that is useful for decision-making for present and potential investors", a formulation that could usefully be inserted in an amended Constitution as a substitute for the above.

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?

Experience suggests that it is impossible for accounting standard-setters to internalize all potential public policy concerns without dramatically lowering the quality of their standards and of the corresponding accounting practices. Furthermore, as global standards, IFRS cannot possibly integrate the diversity of public policy approaches in the world's numerous jurisdictions. Financial stability, in particular, is understood differently in different local contexts, partly as a function of political history and regimes, financial development, and attitudes to risk.

[6] IFRS Foundation Monitoring Board, "Consultative Report on the Review of the IFRS Foundation's Governance", 7 February 2011, available on www.iosco.org

[7] IFRS Foundation Monitoring Board, "Statement of the Monitoring Board for the International Accounting Standards Committee Foundation on Principles for Accounting Standards and Standard Setting", 22 September 2009, available on www.iosco.org

Thus, financial stability concerns are a valid element to be taken into account in jurisdictional frameworks for the adoption of IFRS, such as the one that exists in the European Union[8]. But they should not be referred to as part of the Foundation's own mandate.

Governance

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?

Some important shortcomings of the current structure are analyzed at more length in my response to Phase 1 of the latest Constitution Review (see reference in footnote 4). The core flaw is not the number of tiers, but the hybrid status of the Monitoring Board which both pertains to the Foundation's Constitution framework and is established independently of it. This creates intractable problems of accountability. In my view, two solutions can be envisaged: either making the Monitoring Board an integral part of the Foundation, which means merging its Charter and the existing Memorandum of Understanding into the Constitution; or re-establishing the independence of the Foundation vis-à-vis the Monitoring Board, which would require in particular depriving the Monitoring Board of its current right of veto over Trustee appointments and reappointments. In the latter option, the Trustees would be reestablished as the Foundation's supreme body and duly empowered. In the former option, the relevance of the Trustees as a useful tier of governance would depend on the way the Monitoring Board itself would be redefined by the modified Constitution.

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?

As implied above, it is not self-evident that the Trustees are currently the "primary governance body" of the Foundation, as their own appointments and reappointments are subject to the veto of the Monitoring Board. This mechanism arguably makes the Monitoring Board the de facto "primary governance body" of the IFRS Foundation.

The question asked cannot be considered in isolation and is profoundly linked to the one about which stakeholders' needs IFRS standard-setting should serve in priority, as discussed above in the response to Question 1. If, as I believe is desirable, investors' needs are the Foundation's primary concern, then accountability to public authorities should be framed primarily as a proxy for accountability to the global investors' community (in echo to the mandate of most securities regulators to protect investors at the

[8] Regulation No. 1606/2002 of the European Parliament and the Council of 19 July 2002 (available on www.eur-lex.europa.eu) lists as an adoption criterion that standards should "be conducive to the European public good", a concern that can be interpreted as including requirements for financial stability insofar as they are in the European public interest.

level of individual jurisdictions). This would call for a redesign of the Monitoring Board in a way that would make it better represent the global investors' community.

Process

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?

I believe there has been significant progress in recent years in terms of formally defining the IASB's due process. The problems that have arisen are of execution rather than of definition of the process. An important example is the amendment to IAS 39 adopted in mid-October 2008, which cannot be reasonably considered good standard-setting practice including when taking into account the exceptional circumstances that surrounded it.

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?

Indeed, application and implementation issues will become increasingly important and complex as the use of IFRS spreads around the world. The IFRS Foundation cannot be responsible for adoption and implementation issues in individual jurisdictions, but the "IFRS brand" is bound to be affected by these. One option worth considering would be for the Foundation to monitor adoption and implementation of IFRS in individual jurisdictions, perhaps to the extent of giving public assessments or ratings along both dimensions. Of course, this would require significant resources to be executed in a credible way.

Financing:

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

Financing the IFRS Foundation is a crucial challenge, but I am not sure automaticity should be the objective. Automaticity cannot work without an enforcement mechanism which, in the absence of a global government, can only be provided by governments in individual jurisdictions. Therefore, the requirement for automaticity makes the Foundation ultimately dependent of, and accountable to, individual governments (and the European Union) for its funding purposes, which in my view creates a major tension with the objective of serving the information needs of the global investors' community. The priority should rather be to align, as much as possible, the funding framework with the governance and accountability framework. This may entail a return to a concept of voluntary funding, even though not identical to the one adopted by the Foundation in the early 2000s.

Other issues

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

One important and oft-debated issue is that of the representation of individual jurisdictions in the Monitoring Board. If, as suggested above, the Monitoring Board is seen primarily as an agent representing the global investors' community, then this representation should be considered from the point of view of the investor side rather than of the issuer side. In this view, the fact that a jurisdiction has adopted IFRS fully, partly, or not at all, should be largely irrelevant to the legitimacy of its participation in the Monitoring Board. Similarly, the public institutions that participate concretely in the Monitoring Board should be those in charge of enforcing the quality of financial reporting in their respective jurisdictions rather than those in charge of setting or adopting the standards, to the extent that they are distinct.

As stated earlier, I look forward to the next steps of this important public debate and remain at your service in case you would see an interest in any additional contributions to it.

Yours sincerely,

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