BUSINESSEUROPE

EFRAG
35 Square de Meeûs
B-1000 Brussels

14 July 2011

Dear Sir or Madam,

Re: <u>EFRAG Discussion Paper "Considering the Effects of Accounting Standards"</u>

We have noted with interest the publication of the Discussion Paper regarding the effects of accounting standards. Our comments are set out in the appendix to this letter.

As you can see, while we welcome the paper as a useful first step in what is an important debate, we are not convinced by some aspects of it. We would therefore urge that the next step is focused on discussing potential practical ways of establishing, observing and measuring the various effects an accounting standard might have. In addition, we believe that focus should be on identifying potential cost effective mechanisms to undertake reasonably independent effects studies.

We remain at your disposal should you wish to discuss this further.

Yours sincerely,

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ANNEX

Need for Effects Analysis

We are completely in agreement with the thrust of the DP on the vital need for a continuous process of effects studies and strongly support it. As you are aware, BUSINESSEUROPE sees accounting standards as a means to an end, namely optimal communication of decision-useful financial information between preparers and users as well as within entities. The development of accounting standards has no justification unless it serves that end, and standards are not an end in themselves. This naturally implies that consideration of their effects is absolutely central to their development, and therefore, consideration of the effects must be given a key place in the overall development process. This must indeed start before any development is actually done, at the agenda-setting stage, since standards can only serve a purpose through their positive effects.

We therefore strongly believe that no work on the development of a new accounting standard should even be contemplated unless the expectation of effects has been defined, assessed and exposed for public comment. This assessment must be repeated throughout the process as actual outcomes may – and often do – diverge from original expectations. This is necessary to ensure that the initial assessment still holds or that the current project continues to provide the necessary net positive effects. Since standards are not an end in themselves, the effects studies should provide an unequivocal answer to the question: "Why do we need to change anything and how is this going to impact future reporting?"

We also believe that expected benefits should be demonstrable, with the onus on proving that a change is worthwhile, as we noted all too often an approach to disclosures based on an implicit assumption that more disclosure must per se be useful. (There is doubtless a link into the Disclosure Framework project here.) We regard this as being essential if countries are to accept standards developed at an international level. Finally, the improvements should be mainly for the benefit of existing IFRS applicants and the prime users of their financial statements rather than solely for the ease of future adopters.

Carrying out effects studies ex post, as was done with IFRS 3, is clearly just too late in the whole process to avoid inefficient use of resources and other dysfunctional impacts.

Some aspects for re-consideration

However, while we agree with the DP on the importance of effects, we do nonetheless have doubts about some of the DP's suggestions. Generally, we wonder to what extent the proposed approach, though theoretically fine, is workable in practice and therefore believe that more work will be needed on this. For instance, to what extent is it practical to determine system change and running costs in the very early agenda-setting and planning phases where the shape of the final standard is still ill defined?

While we understand that resources should be used in an efficient and productive way, we certainly do not agree that the depth of analysis work "should be proportionate to … the time available.", especially at the early stages of a project when it is especially necessary to be clear on the implications of change [2.19] This is too easy a get-out, and the annual improvements process illustrates how the views on how material a change might or might not be have significantly diverged in the past. From our perspective, there is a concern that there is never enough time in the development process of a new standard, especially towards the end of a project, but lack of it – particularly against the standard setters' own timetables - should not be allowed to detract from a solid assessment. What are often perceived to be artificial deadlines set by standard setters should not be rigidly adhered to if it is at the cost of issuing standards which have unfortunate and undesirable consequences. The depth of the analysis should at least be in balance with the relevance, complexity and implementation effort associated with the proposals.

Responsibility for performing Effects Analysis

The DP suggests that it is the IASB which should be carrying out the effects studies. We disagree with this conclusion. The IASB currently has neither the skills and knowledge of practical application nor, more importantly, the essential independence to do this satisfactorily. Under other approaches we accept that it might be the case that the benefits identified in paragraph 2.10 of the DP would not fully materialise. However, we believe that having an interested party (which the IASB clearly would be) perform the study would be a significant breach in the "checks and balances" approach to which a standard setter and its pronouncements should be subject and could potentially impair the credibility of such effects analysis.

Consequently, if there were to be only one party responsible for the studies during the whole project, then we believe that the studies **must** be done by a body independent of the IASB and its staff. Further deliberation is needed to determine whether that independent body might be some organisation under the IFRS Foundation or whether it should be independent of that structure. It may however be possible that at different stages of the development process, as identified in paragraph 2.14 of the DP, different parties could be involved, with the IASB e.g. being responsible during the planning phase or the discussion paper phase. Further, the due process to be applied must be clear and explicit, for instance laid down in a manual, and this should perhaps itself be subjected to review at regular intervals in the light of experience.

Focus of Effects Analysis

We accept the DP's point about not *restricting* the concept of "effects" solely to "costs and benefits". [3.2 et seq.] Nevertheless, costs and benefits are essential factors in the proper assessment of effects (including those on "the public interest"), even if they are difficult to quantify, especially in the case of benefits. As preparers we have been disadvantaged for too long under what some would regard as too cavalier an approach to preparers' costs in the standard-setting process. Even if entities already have staff that can be deployed on the preliminary analysis of the impacts and necessary changes as well as the implementation of changing accounting standards, there is still an opportunity cost as they are diverted from other work. There is also that oft neglected potential cost to users where changed standards are such that the preparation of financial reporting can no longer be managed acceptably within the current time-scales and users must thus bear a delay in obtaining topical information. We would therefore recommend that any formal procedures on effects studies should still mention such costs *explicitly,* as key elements always needing to be considered in the assessment of effects. Establishment of some agreed bases (e.g. marginal or full costs, etc.) could help to facilitate at least an approximate or indicative quantification. Furthermore, it would be advisable to develop a short, non-exclusive list of other effects that need to be addressed in order to create consistency across individual studies.

It must also be made clear that *all* the costs of a project for preparers and users, whether initial implementation or on-going, need consideration and that such important aspects as staff-training for both preparers *and* users should not be omitted.

Furthermore, preparers are a key user, and where standards potentially diverge from the approach used by entities to manage their businesses, the costs and benefits of planned changes need particularly careful review to ensure that they would actually be of practical use for preparers and users and not just satisfying for academics and theoreticians.

At an overall level, we find this part of the DP needs further development and is on several occasions rather vague. In addition to the comments made above, the DP for example discusses the terms “positive, negative and neutral”, but does not explain at all how the assessment should be made. The DP also spends some time discussing the difference between “marginal effects and absolute effects” but does not give any helpful examples or any indications how these effects should be observed and measured. We also find the two paragraphs on “anticipated effects and actual effects” to be rather vague, and it remains unclear at this point (3.28 et seq.) what the position of the DP is and how the distinction would play a role in the overall effects analysis.

In this context, we would also reiterate the concerns we and others have expressed over the danger that financial statements become increasingly cluttered in response to the demands of various special interest groups adding disclosures unrelated to the prime aim of financial statements.

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