

20 September 2012

Michel Prada  
Chairman  
IFRS Foundation  
30 Cannon Street  
EC4M 6XH London  
United Kingdom

Dear Mr Prada,

**Re: IASB and IFRS Interpretations Committee Due Process Handbook**

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Invitation to Comment *IASB and IFRS Interpretations Committee Due Process Handbook*.

EFRAG welcomes the review of the Due Process Handbook. EFRAG appreciates the efforts that the IFRS Foundation and its Due Process Oversight Committee have made to improve the due process of the IASB and the IFRS Interpretations Committee. We are pleased to notice that the proposed Due Process Handbook addresses a number of concerns raised previously by EFRAG.

We believe that the principles based approach adopted in the revision of the IASB's due process based on transparency, full and fair consultation and accountability, is essential in order to avoid that the due process would merely result in a "ticking the box" exercise. The IFRS Foundation should therefore be cautious of adding too much detail into the Due Process Handbook that would undermine the principles based character of the standard setting process and leave no room for any flexibility in the due process. In our view an appropriate balance should be found between a principles based due process and the assurance of compliance.

**Defining the objectives of the IASB's due process**

EFRAG would welcome if the Due Process Handbook explains the objectives of the due process. The Due Process Handbook sets out the underpinning principles without addressing the overall objectives of the due process. In EFRAG's view the IASB's due process plays a fundamental role in supporting legitimacy and acceptability of IFRS. EFRAG suggests that the following objectives should be set:

- i) Ensuring a **shared identification** with constituents of well defined needs for improvement of financial reporting, in a way that allows clarity in how objectives assigned to a project are set;
- ii) Allowing for **proper consultation and discussion**, prior to, and after, the publication of proposals;

- iii) Setting the legitimacy of the resultant standards or interpretations by gathering **arguments** and reference to **evidence** in a basis for conclusions that:
- a. **justify** (and not assert) how the new requirements do indeed fulfil the original objectives and serve user needs;
  - b. **explain** how specific issues raised by various jurisdictions/ constituents have been addressed;
  - c. **argue** why alternatives supported by constituents would not achieve the same outcome or why the final requirements should be preferred;
  - d. properly **assess** the results of effect studies and other field work including field tests, so that there is reasonable assurance that implementation of the final requirements will not cause uncertainty or inconsistency in practice, and that the costs involved are justified by the improvements brought in financial reporting.

### **Agreeing principles for the IASB's due process**

EFRAG supports that principles be set to govern the IASB's due process and supports the three underlying principles on which the due process requirements are built: the principles of transparency, full and fair consultation, and accountability. Those principles should be met to ensure that the objectives suggested above are fulfilled.

However, the overarching principle that is assigned to the work of the IASB is to bring **improvement to financial reporting at an acceptable cost**, where needs for improved or for revised or new accounting requirements have been evidenced. This principle **should be the sole driver** for changes to standards and for interpretations. The dedication of the standard setting process to improvement to financial reporting should be reflected at all stages.

### **Improving the proposals for the standard setting process**

To help fulfil the objectives of the IASB's due process that we have detailed above, we formulate comments and recommendations below. More detailed comments are provided in the appendix 1 to this letter.

#### **1- We welcome the research programme in coordination with accounting standards bodies and others, that has been introduced in the IASB due process and that reflects recommendations we have made at the time of the IFRS Foundation Strategy Review.**

The introduction of the research programme phase in the standard setting process is an important step forward in achieving evidence based agenda setting following public consultation, as EFRAG recommended earlier. The research programme phase should always be concluded by a public consultation phase on the issue and the possible approaches considered to address the issue before deciding to add a project to the standard-setting programme. The findings and conclusions reached as a result of this public consultation on the discussion paper or research paper, demonstrating that changing the requirements would lead to improved financial reporting at acceptable cost should be publicly available. EFRAG therefore recommends that the need for this public consultation leading to shared identification of what improvements are needed, and their level of priority, if any, be introduced in the IASB' due process.

This will have the supplementary merit of prioritising the IASB work programme on the basis of the needs of those who apply IFRS in practice. EFRAG believes indeed that amendments to IFRS aiming at attracting potential new IFRS adopters should not be at the expense of existing users of IFRS.

**2- We would like to promote a shared due process between the IASB and regional and national accounting standards bodies.**

Involving, and coordinating with, regional and national accounting standards bodies in IASB's technical activities in the research programme phase, in outreach activities and field testing, in post-implementation reviews and other surveys is an effective way to improve transparency, efficiency and mutual understanding of the standard setting process. Feedback statements such as those published by EFRAG are necessary to fulfil the transparency principle. We are therefore pleased to see that the IASB identifies regional and national accounting standards bodies as key contributors to the IASB's due process, from research phase to post-implementation review. We recommend that shared due process be identified as the way forward.

**3- We believe that effect analyses are essential components of the IASB decision making process and should be integrated into the standard setting due process over the life-cycle of projects.**

Effect analysis should be integrated into the standard setting due process over the life-cycle of projects. Effect analysis brings a means to challenge tentative decisions in their capacity of bringing the envisaged improvements. Effect analyses are not only a matter of accountability: they are an essential component of the IASB decision making process. It is therefore important that the Board is involved in effect analyses, considers the results of such analyses in public meetings and reflects those results in its decisions. As stated in the UK ASB and EFRAG Position Paper *Considering the Effects of Accounting Standards*, Effect analysis should be undertaken for all new accounting standards and major amendments and have more prominence in the proposed Due Process Handbook. The analysis work should follow the principle of proportionality in terms of the degree of analysis work undertaken and the work should be adjusted to the scale of anticipated effects. The burden for preparers is to be taken into account as their input is essential.

**4- We believe that the Due Process Handbook should set guiding principles to apply to how the IASB identifies and analyses users' needs.**

The Due Process Handbook should establish the link with the objective as defined in the IASB's Conceptual Framework and develop some guidance as to how users' needs should be identified and analysed. To that purpose, we think that the notion of users' needs should be better developed. Hence, the perspective of securing long term stakeholder value aligns in many cases the views of buy side analysts, longer term oriented users and preparers in their stewardship responsibilities. We welcome the current efforts of the IASB in consulting a wider range of users beyond sell-side analysts. Also the diversity of users' needs is such that users' needs should not be assessed in terms of "what users wish or want" but in terms of "what users need and why and for what purpose". Users should have to justify their views as other participants in the IASB's due process are expected to do. The IASB due process should also provide more room for meetings involving investors' representatives and management's representatives as financial reporting is primarily a communication and accountability tool between those two groups. In this respect we believe that the meetings organised between the IASB Capital Markets Advisory Committee and the Global Preparers Forum are a good model that could be applied more generally.

**5- We believe that results of public fatal flaw reviews, and when appropriate of field tests, should be assessed, in a public meeting, before the IASB makes its final decision on a standard or amendment.**

Defining robust accounting requirements is necessary, but not sufficient, to foster improvement in financial reporting. Review drafts published for systematic public ‘fatal flaw’ reviews are essential in the identification of potential implementation difficulties or undue costs, and should serve as a basis of ultimate field tests when appropriate. Moreover the responsibility for assessing the results of such steps should not rest with the staff, but with the Board. The IASB should consider the findings and outcomes of such reviews in a public meeting (with appropriate supporting papers) and the IASB should take the result of the reviews into account when making final decisions.

**6- The IASB staff should support the decision making process of the IASB, albeit never in a position of direction or decision.**

The roles of the IASB and its staff should be clearly distinct. In our opinion IASB is responsible for decision making and for leading the standard setting process in general. The staff should ensure that all the relevant opinions and concerns including the relevant voices of smaller groups of stakeholders and individual jurisdictions, in particular of those that apply IFRS, are brought to the attention of the IASB in a fair and balanced way and are taken into account. Staff should respect the results of due process and respect the Board’s discussions that already took place unless new developments would emerge. Staff is welcome to make recommendations, but after having prepared a fair and balanced representation of various views. The IASB should provide proper directions to the staff in the standard setting process.

**7- While ultimate approvals remain with the IASB, the IFRS Interpretations Committee should be an important partner in standard setting.**

While we agree that interpretation of IFRS should not introduce contradictions with current IFRS, interpretations should also contribute to more useful financial reporting. Achieving greater consistency in practice contributes to greater comparability; however, this should never be at the cost of relevance. We welcome the requirement that the IFRS Interpretations Committee should refer its conclusions to the IASB when it believes that an IFRS or the Conceptual Framework should be modified. The outcomes of every possible consensus should be assessed against qualitative characteristics of useful financial information as defined in the Conceptual Framework. Whenever concerns arise, the issue should be referred back to the IASB.

We observe that no discussion arises at the IASB level when an interpretation is presented for approval. The discussion takes place at the IFRS Interpretations Committee level. Therefore the process of coming to a proposed or final interpretation would be more transparent if the IFRS Interpretations Committee members voting against would be required to publicly explain why they have a dissenting view. This is particularly important in the consultation phase.

**8- We urge the Trustees to clearly stipulate that the IFRS Interpretations Committee should not issue any rejection notice that would be akin to an interpretation.**

While we understand the reasoning followed by the Trustees in their considerations of the rejection notices, we believe that reaffirming that rejection notices have no authoritative status is not enough. In practice, regulators do refer to rejection notices in the exercise of their enforcement responsibilities. ESMA in Europe operate in the expectation that rejection notices are part of the IFRS literature to which preparers should refer. As a result, the Due Process Handbook should clearly indicate that rejection notices should not be akin to interpretations and quality control by the IASB should be reinforced before final issuance, more especially when they raise controversy. The IASB should in its dialogue with auditors and regulators ensure that the status of rejection notices is well understood and that auditors and regulators refrain from giving rejection notices an inappropriate status.

**9- We believe that every decision made in the standard setting process should be subject to the super majority required for the whole standard.**

All jurisdictions which have adopted IFRS expect that the IASB develops high quality financial reporting standards and interpretations. We agree that standards should be approved in the formal existing balloting systems in place at the IASB, and that the IASB members are asked to assess if the final standard fulfils the overarching objective of improving financial reporting at a reasonable cost, providing an overall assessment at that stage.

We believe, however, that the current decision making process leaves too much room for defects or shortcomings. This stems from tentative detailed decisions being made on the basis of a simple majority, in the course of the project, without having a quorum in IASB meetings.

These defects and shortcomings – or as a minimum, controversies - that can be avoided, and do not affect the general thrust and consistency of the final standard, represent potential difficulties (or at the minimum offer room for the request of exceptions upon endorsement) in the various endorsement processes that most jurisdictions have adopted. We therefore believe that the super majority that is needed to approve of a standard should be required for all decisions made in the process of developing the standard, or any other change in the due process that would achieve a similar outcome.

**Considering due process oversight**

We welcome the efforts developed by the IFRS Foundation in its due process oversight responsibilities, and the choice to make it an ongoing process. Those efforts satisfy EFRAG's longstanding requests. However we re-emphasise that the focus of the due process oversight responsibility should be on substance, and not on form, so that the Due Process Oversight Committee (DPOC) ensures that the objectives set for the IASB's due process are indeed met.

We welcome that a function, Director for Trustees' activities, has been created. We believe this will bring to the DPOC the means in dedicated staff that it needs to lead its independent review.

Appendix 1 to this letter elaborates the issues raised in this cover letter and provides additional comments on issues not specifically raised in the questions in the Invitation to Comment. Appendix 2 provides responses to the questions included in the Invitation to Comment.

Should you like further clarification of the points raised in this letter, please do not hesitate to contact Robert Stojek, Didier Andries or me.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Pedro Solbes', with a small horizontal line at the end.

Pedro Solbes

Chairman  
EFRAG Supervisory Board

## Appendix 1

### EFRAG'S MAIN COMMENTS ON THE DUE PROCESS HANDBOOK PROPOSALS

1. EFRAG supports that principles be set to govern the IASB's due process and supports the three underlying principles on which the due process requirements are built: the principles of transparency, full and fair consultation, and accountability. Those principles should be met to ensure that the objectives suggested in the covering letter are fulfilled.
2. However, the overarching principle that is assigned to the work of the IASB is to bring **improvement to financial reporting at an acceptable cost**, where needs for improved or for revised or new accounting requirements have been evidenced. This principle **should be the sole driver** for changes to standards and for interpretations. The dedication of the standard setting process to improvement to financial reporting should be reflected at all stages.

#### *Shared due process*

3. The proposed Due Process Handbook indicates that the due process requirements are built on the principles of transparency, full and fair consultation and accountability. We share the views of the IFRS Foundation that a comprehensive and effective due process is essential to developing high quality IFRS. We welcome that in paragraph 3.48 the IASB in its technical activities seeks input from a network of regional and national accounting standards bodies. These bodies can undertake research, provide guidance on the IASB's priorities, encourage stakeholder input from their own jurisdictions into the IASB's due process and identify emerging issues.
4. We welcome the cooperative spirit expressed in the Due Process Handbook but believe that the IASB should make further efforts and move to a shared due process with the regional and national accounting standards bodies in order to avoid over soliciting of stakeholders on the same subject by different organisations. This would mean that in each jurisdiction the stakeholder consultation – be it through field testing, outreach events, surveys, post-implementation reviews or other means - would be coordinated, shared and involve regional and national accounting standards bodies in obtaining the views from stakeholders on a particular subject. In Europe this would notably mean a coordinated effort of the IASB, EFRAG and the National Standard Setters and possibly the regulators.
5. This approach has several benefits. It is more efficient with stakeholders being asked for their views once (stakeholders often claim to be over solicited by the various organisations). It is more transparent with the IASB, regional and national accounting standards bodies listening to the same views at the same time receiving the same information and leaving less room for interpretation. The organisations involved will publish joint feedback statements on the consultations, so that the information received is publicly available. This is an effective way of improving transparency of the standard setting process. Finally, it will lead to an increased mutual understanding as everyone will work with the same information and is involved at the same time.

6. We welcome that the IASB has, in the most recent years, engaged in extensive outreach activities. The outreach activities bring knowledge about the underlying issues justifying concerns or comments in letters received. EFRAG supports these outreach activities as a useful addition to the IASB's due process and appreciate that it has resulted in a more in-depth and thorough re-deliberation process. We think that it would be useful if the transparency that characterises IASB's other activities were extended to such outreach. For example, where additional contacts and meetings have been organised to reach users, information on who took part in which activities or events, and what were the results of those activities or events, should be publicly available.
7. Recent experience suggests that the IASB on the one hand and the regional and national accounting standards bodies on the other can draw different lessons from similar due process steps, leading to a lack of mutual understanding. This could be receded by enhanced cooperation in this area.
8. EFRAG has taken the initiative in 2010 to coordinate outreach activities with the IASB and the National Standard Setters in Europe. Such initiatives proved to be effective, as all the involved bodies and constituents may meet face-to-face on one event that is followed-up by a public feedback statement prepared jointly and with a general consent.
9. However, we wish to underline that in our experience such outreach initiatives can only be effective if the results are made publicly available and if the following conditions of cooperation are met:
  - a. There is a need to have commonly agreed rules between the organisations involved for the organisation, structure and contents (including supporting material) of the events.
  - b. The events should be publicly announced with public invitations for participation.
  - c. The events should be held in English or in national language with an English simultaneous translation provided. The results should be made public at least in English in order to ensure that all who wish so, have access to this information.
  - d. The basic documentary evidence resulting from the event should be shared between the organisations involved and public feedback statements should be issued.

In our view, the cooperation should proceed along these lines but this should not end up impeding progress in the outreach events.

10. In conclusion, we are pleased to see that the IASB identifies regional and national accounting standards bodies as key contributors to the IASB's due process, from research phase to post-implementation review. We recommend that shared due process be identified as the way forward.



## **Due process documents**

### *Field testing*

11. The Due Process Handbook refers to field work which includes but is not limited to field testing. EFRAG finds the inclusion of field work in the standard setting process very important. However, in the paragraph below, we will focus specifically on field testing – i.e. asking practitioners to apply the proposed or pre-final requirements to real transactions and users to assess whether financial reporting outcomes are useful – where we think there is an opportunity for further improvement.
12. We welcome the integration of field tests in the Due Process Handbook. Field tests are important to ensure that proposed accounting requirements are reasonably easily understandable and capable of being implemented at operational level. We firmly believe that field testing results should be considered in the development of all major changes to standards.
13. Field testing answers a number of questions such as (i) is the standard operational, (ii) what is the cost of implementation of the standard, (iii) is the standard difficult to apply or not. We strongly believe that the results of field testing should be an integral part of the IASB decision making process and should be publicly available: this requires that field tests are conducted while their results may be reflected in the standard.
14. EFRAG has in cooperation with the National Standard Setters run some field tests with positive experiences for contribution to the standard setting process. We believe that it is likely that, at least in Europe, there will be a greater demand for field tests prior to endorsement decisions on final standards and interpretations. As part of the shared due process, we believe that it is essential that field tests are organised jointly by the IASB and regional and national accounting standards bodies, as an integral part of the IASB decision making process.

### *Review drafts*

15. We welcome the use of public review drafts as this gives the constituents the possibility to see the ‘final’ text and still to be able to contribute to further clarification of the text and to use the review draft for field testing. Review drafts published for systematic public ‘fatal flaw’ reviews are essential in the identification of potential implementation difficulties or undue costs, and should serve as a basis of ultimate field tests. We believe that review drafts should always be made publicly available and not only at the discretion of the IASB. We therefore do not support paragraph 3.29, which indicates that “a review draft might be distributed to a selected group of reviewers”. While public fatal flaw reviews should be performed systematically, ultimate field tests should be run more particularly when the changes are significant or when controversy has arisen as to potential implementation difficulties or relevance of reporting outcomes.
16. We believe that the due process in relation to review drafts needs to be further developed. We believe that the IASB should consider the findings and outcomes of such reviews in a public meeting (with appropriate supporting papers). The IASB should take the result of the reviews into account when making the final decisions.

17. In our view final balloting should only take place on the final draft including the results of the public 'fatal flaw' review. We therefore disagree with paragraph 3.31 where it is said that "the staff must also decide whether a review draft should be developed before the first pre-ballot draft is circulated to IASB members or whether one of the ballot drafts should be used for this purpose". We stress that the standard setting process be entrusted to the IASB, not to staff, and staff should support the IASB in its work and make recommendations, but have no steering or decision making role.

### *Effect Analysis*

18. Effect analysis should be integrated into the standard setting due process over the life-cycle of projects, starting from the agenda proposal stage through to post-implementation reviews. We welcome the inclusion of the effect analysis in the standard setting process. Effect analysis brings a means to challenge tentative decisions in their capacity of bringing the envisaged improvements. However, we want to underline that effect analyses are not only a matter of accountability: they are essential components of the IASB decision making process. It is therefore important that the Board is involved in effect analyses, considers the results of such analyses in public meetings and reflects those results in its decisions.
19. As stated in the UK ASB and EFRAG Position Paper *Considering the Effects of Accounting Standards*, Effect analysis should be undertaken for all new accounting standards and major amendments, but the analysis work should follow the principle of proportionality in terms of the degree of analysis work undertaken. Therefore, work should be adjusted to the scale of the anticipated (or intended) effects. Also, when integrating the effect analysis in the standard setting process the burden for preparers is to be taken into account as their input is essential. The main messages and recommendations in the Position Paper are supported by twelve European National Standard Setters.
20. Results of the effect analyses should also be publicly available prior to the IASB making decisions and not after the fact as a supplementary duty accompanying publication and should be taken into consideration and referred in the decision making process. We therefore do not support paragraph 3.73 that seems to indicate that the results of the effect analysis are summarised in a separate effects analysis publication when the IFRS is issued. In our view, the indication in paragraphs 6.6. and 6.22 that the staff has considered the likely effects of the proposals or the new IFRS is not meeting our concerns since we believe that the Board members should themselves assess the likely effects.
21. In paragraph 3.72 it is stated that the likely effects are assessed in the light of the IASB's objective of financial reporting transparency; and in comparison to existing financial reporting requirements. In paragraph 3.74 in our view, a too narrow focus is taken in describing how the Board should form its judgement on the evaluation of the likely effects. We believe that the Board should also consider the effects other than on financial reporting that a change to a standard or a proposed standard or interpretation can have. Our concerns also relate to paragraph 3.79 where the text implies that the decision making is based on whether the new requirements will improve financial reporting taking into account the likely effects of those requirements. Clearly the consideration of effects should be wider than financial reporting.

22. In this respect we refer again to the UK ASB and EFRAG Position Paper *Considering the Effects of Accounting Standards*: “the standard setter should endeavour to be aware of effects that go beyond the objective of the standard setter, such as macro-economic effects (e.g. financial stability impacts, the more efficient allocation of resources, redistributive effects within society, etc.). The standard setter should also make information about expected macro-economic effects publicly available so that relevant bodies can take action. In some cases it might also be appropriate for the standard setter to communicate an issue that has been identified directly to a relevant body.”

#### *Decision making*

23. The IASB should ensure that all possible divergent views are taken into consideration in the standard-setting process including views expressed by minorities, individual jurisdictions, industries and stakeholder groups and provide proper reasoning why views are not taken into account.
24. We are fully aware that the IASB, as a global standard setter, maintains interactions with constituents all over the world and in this process receives input for further improvement of IFRS from many organisations and bodies. In dealing with this input however, we believe that a well justified balance should be found to hear and assess all the relevant voices. The IASB should ensure that amendments to IFRS aiming at new applicants of IFRS are not at the expense of existing users of IFRS. On the contrary, in certain parts of the standard setting process such as agenda setting and field testing more weight could be given to requests and inputs from constituents and jurisdictions applying IFRS.
25. We believe that it also needs to be clarified how proportionality is applied in assessing the comments received not only in terms of jurisdictions but also in terms of comments received from organisations versus comments received from individuals.
26. The dedication of the standard setting process to improvement to financial reporting should be reflected at all stages; at the outset, any change to current standards should be based on a shared identification of whether and where improvement is needed. Justifications of how proposals are appropriate to meet set objectives should be properly provided, and not only be based on what IASB members believe, think or assert. A recent example where the rationale of a decision is difficult to follow is that it was argued that unbundling of insurance contracts brings transparency to financial reporting, and at the same time it was argued that bifurcation of hybrid financial assets should not be introduced, for reasons of simplification and because a financial instrument was a whole contract that should not be unbundled.

#### *Supermajority for all decisions in the development of a standard*

27. All jurisdictions which have adopted IFRS expect that the IASB develops high quality financial reporting standards and interpretations.
28. We agree that standards should be approved in the formal existing balloting systems in place at the IASB, and that the IASB members are asked to assess if the final standard fulfils the overarching objective of improving financial reporting at a reasonable cost, providing an overall assessment at that stage.

29. We believe, however, that the current decision making process leaves too much room for defects or shortcomings. This stems from tentative detailed decisions being made on the basis of a simple majority, in the course of the project, without having a quorum in IASB meetings.
30. These defects and shortcomings – or as a minimum, controversies - that can be avoided, and do not affect the general thrust and consistency of the final standard, represent potential difficulties (or at minimum offer room for the request of exceptions upon endorsement) in the various endorsement processes that most jurisdictions have adopted. We therefore believe that the super majority that is needed to approve of a standard should be required for all decisions made in the process of developing the standard, or any other change in the due process that would achieve a similar outcome.
31. The IASB would serve better its strategy of promoting IFRS “as published by the IASB” if every decision with respect to a standard was subject to the super majority required for the whole standard. We therefore suggest paragraphs 3.78, 3.79 and 3.80 to be amended accordingly.

***Longer term perspective: users and preparers***

32. Acceptability of IFRS standards, and quality of financial reporting overall, would be better served if the somewhat artificial dichotomy opposing benefits for users and costs to preparers was abandoned. Costs incurred in the preparation of financial reporting could potentially erode shareholder’ value. Preparers are exercising their stewardship responsibility towards shareholders when they provide their views to the IASB. Financial reporting is essential to them to discharge their stewardship responsibilities.
33. Improved financial reporting serves potential and existing shareholders, both being interested in as effective financial reporting as possible. Existing shareholders are interested in being able to assess management’s stewardship. In this respect we welcome the emphasis put by Hans Hoogervorst in his speech in June 2012 in Amsterdam on true investors, those that actually own assets. As indicated earlier in our Comment Letter dated 5 August 2011 on the report of the Trustees Strategy Review EFRAG believes that the IFRS Foundation objective should be more precisely directed to providing financial reporting that is best suited to serve sound economic growth and sustainable value creation, and based therefore on a long term perspective of involvement with the reporting entity. Transparent financial reporting is indeed crucial to securing long term stakeholder value and in our view does thus also include the concept of stewardship in that management should demonstrate how it has discharged itself of its stewardship duty to ensure the long term sustainable wealth creation. The perspective of securing long term stakeholder value aligns in many cases the views of buy side analysts, longer term oriented users and preparers.

34. EFRAG therefore believes that the IASB due process should concentrate more widely on improvement of financial reporting meeting those users' needs. However, we think that the notion of users' needs should be better developed and it should be clarified how "users' needs" are expected to be evaluated and on what bases. The diversity of users' needs is such that users' needs should not be assessed in terms of "what users wish or want" but in terms of "what users need and why and for what purpose". The IASB due process should also provide more room for meetings involving investors' representatives and management's representatives as financial reporting is primarily a communication and accountability tool between those two groups. We welcome the current efforts of the IASB in consulting a wider range of users beyond sell-side analysts.
35. A rigorous analysis of users' and preparers' needs would be a significant enhancement in the transparency of IASB's decisions. The needs of users and preparers are to be balanced in defining the accounting standards. Only in this way, a deliberation of information needs can demonstrate whether the final standard or amendment to an existing standard represents a balanced view and results in improved financial reporting.

#### ***Respective responsibilities of Board and staff***

36. Under the heading 'Assigned IASB members' the proposed Due Process Handbook indicates in paragraph 3.39 that for major projects, the Chair of the IASB normally assigns specific IASB members to the project. In our opinion it would be very useful to make this decision (and any changes to this decision) publicly available. We believe that this information should be available on the dedicated webpage of a particular project.
37. Following paragraph 3.39 "assigned IASB members provide advice to the staff on the adequacy and clarity of the analysis presented in drafts of staff papers to ensure that sufficient information needed for the IASB to make technical decisions is presented". Notwithstanding that it is also mentioned that "the recommendations made in staff papers do not necessarily reflect the views of the assigned IASB members and the staff have ultimate responsibility for the board papers and recommendations they contain".
38. We believe that roles of the IASB and its staff should be clearly distinct. In our opinion IASB is responsible for decision making and for leading the standard setting process in general. The staff should ensure that all the relevant opinions and concerns including the relevant voices of smaller groups of stakeholders and individual jurisdictions, in particular of those that apply IFRS, are brought to the attention of the IASB in a fair and balanced way and are taken into account. Staff should respect the results of due process and respect the Boards discussions that already took place unless new developments would emerge. Staff is welcome to make recommendations, but after having prepared a fair and balanced representation of various views. The IASB should provide proper directions to the staff in the standard setting process.

39. An example of undue influence of the staff on the Board decision making process is the discussion on bifurcation of financial assets. At a moment when the IASB and FASB Boards had already agreed to converge their standards on classification and measurement of financial instruments (a decision taken after following the internal due process), the staff still challenged this by starting the bifurcation debate all over again, proposing no bifurcation at all.
40. We therefore advocate for a clarification of the responsibilities and roles of the Board members and the staff in the Due Process Handbook.

### ***IFRS Interpretations Committee***

#### *Transparency of submissions to the IFRS Interpretations Committee*

41. At this moment there is no clarity who submits issues to the IFRS Interpretations Committee. We believe that more transparency is needed in this area. Whilst we appreciate that submitters may prefer confidentiality for different reasons, we suggest that to facilitate the understanding of the context in which the issue arose the type of submitter (preparer, auditor, regulator, etc) and the country of origin are made publicly available.

#### *Relevant financial reporting*

42. We recognise the role of the IFRS Interpretations Committee as a body that along with the IASB is responsible for maintenance of IFRS and especially has as an objective to interpret the application of IFRS and to provide timely guidance, following the requests of its constituents if divergent accounting practices have emerged. However we have to highlight some of our concerns about the process of developing an interpretation.
43. Firstly we are of the opinion that the IFRS Interpretations Committee should not satisfy itself with a consensus solely based on where relevant existing IFRS seem to lead to. We note that paragraph 5.17 refers to a principle-based approach founded on the Conceptual Framework. In our view this means that the outcomes of every possible consensus should be assessed against financial reporting qualitative characteristics as defined in the IFRS Framework. We believe that this should be an explicit requirement of the Due Process Handbook rather than the general reference as included in paragraph 5.17. An example where reasoning on the basis of consistency with existing requirements resulted in an inappropriate interpretation is emission rights (IFRIC 3).
44. In its final negative endorsement advice on IFRIC 3 EFRAG concluded that applying IFRIC 3 would not always result in economic reality being reflected and relevant information being provided, because the accounting required in IFRIC 3 was constrained by the interpretation of the interplay of the existing standards IAS 38, IAS 20 and IAS 37.

45. We welcome the requirement in the proposed Due Process Handbook in paragraph 5.20 when the IFRS Interpretations Committee believes that an IFRS or the Conceptual Framework should be modified, or an additional IFRS should be developed, it refers such conclusions to the IASB. We believe that it is crucial if the existing requirements result in an Interpretation that will not provide useful information in particular or does not satisfy qualitative characteristics for relevant financial reporting than no interpretation should be issued and the IFRS Interpretations Committee should refer the issue to the IASB.

*Assessing if issues are widespread*

46. The report on the Trustees' Review of Efficiency and Effectiveness of the IFRS Interpretations Committee proposes revised agenda criteria. It would be helpful if the Handbook could discuss further the criteria of prevalence and significance. We believe that regional and national accounting standards bodies should be involved in assessing whether an issue is widespread and has practical relevance. The Due Process Handbook should therefore explicitly include such a consultation step and regard outreach to national accounting standards bodies and regional bodies as a matter of routine as referred to in the above report.

*Alternative/Dissenting views*

47. We note that the requirements in relation to dissenting views differ for the development of standards and the development of interpretations. Members of the IFRS Interpretations Committee cannot dissent from an interpretation (paragraph 7.19). While we support that the IASB has ultimate authority and responsibility for the interpretations issues, we observe that the analysis and discussion of the issues takes place within the IFRS Interpretations Committee. We see no reason why alternative views would be published accompanying exposure-drafts for standards whereas concerns that have led IFRS Interpretations Committee members to reject the consensus should be reflected as part of the Basis for Conclusions. Transparency and fair consultation would be better served in our view if IFRS Interpretations Committee members' alternative/dissenting views were published. This is particularly important in the consultation phase.

*Rejection notices*

48. While we understand the reasoning followed by the Trustees in their considerations of the rejection notices, we believe that reaffirming that rejection notices have no authoritative status is not enough. In practice, regulators do refer to rejection notices in the exercise of their enforcement responsibilities. ESMA in Europe works on the basis of the expectation that rejection notices are part of the IFRS literature to which preparers should refer. We believe that the Due Process Handbook needs to clarify the process in relation to the rejection notices in that paragraph 5.16 should frame rejection notices in terms of content and avoid that they become in effect additional interpretations. As a result, the Due Process Handbook should clearly indicate that rejection notices should akin to interpretations and quality control by the IASB should be reinforced before final issuance, more especially when they raise controversy.

49. We also think that it is the responsibility of the IASB to keep the common understanding of the status of rejection notices. We suggest the IASB should in its dialogue with auditors and regulators ensure that the status of rejection notices is well understood and that auditors and regulators refrain from giving the rejection notices an inappropriate status.

### **Practice Guidance**

50. With the management commentary guidance as referred to in paragraph 6.36 of the proposed Due Process Handbook, the IASB has entered the area of financial reporting other than financial statements. We understand that the proposed Due Process Handbook must address this type of guidance. However we note that the reference to practice guidance within the section with heading “Finalising IFRS” is misleading, as this type of guidance is not part of IFRS. Moreover using terms similar to implementation guidance that may accompany an IFRS adds to this misunderstanding. We believe that the role of practice guidance should be clarified especially in the context of the standard setting role of IASB and other sources of guidance available. It would be helpful to clarify the status of the Practice Guidance in particular since the Board formally approves the Practice Guidance..

### **Transparency**

51. We believe that meetings of all consultative groups and advisory groups should be public and that supporting documents for those meetings should be publicly available.
52. The voting in the meetings and by other means should be fully transparent and publicly available.

### **IFRS for SMEs**

53. In our view the proposed Due Process Handbook should also cover IFRS for SMEs.
54. In its Draft Comment Letter responding to the Request for Information “Comprehensive review of the IFRS for SMEs” EFRAG acknowledges that between reviews of the IFRS for SMEs, issues could arise that would benefit from further guidance. EFRAG would therefore be in favour of having something similar to the IFRS Interpretation Committee for the IFRS. EFRAG has, however, not been in favour of the procedure applied when issuing Q&As so far since EFRAG believes that the criteria set for the development of Q&As in the SMEIG’s terms of reference were often not respected.



## Appendix 2

### EFRAG RESPONSES TO THE QUESTIONS ASKED IN THE DRAFT IASB AND IFRS INTERPRETATIONS COMMITTEE DUE PROCESS HANDBOOK

#### Question 1 - The Trustees' have included an introductory section dealing with 'oversight', and the responsibilities of the DPOC.

#### Do you support the inclusion and content of this section? Why or why not?

55. EFRAG welcomes the activities of the DPOC and believes that the due process oversight has been improved. We believe that description of the process and responsibilities for oversight of the DPOC in the Handbook brings welcomed transparency in the DPOC duties. However, we believe that the Due Process Handbook may not be the appropriate place to describe the role of the DPOC and believe that the objectives of the DPOC should rather be included in the IFRS Foundation Constitution.
56. We have a number of suggestions for further improvements on due process oversight to provide a better focus on the substance, rather than the form of the due process – i.e. have all underlying principles been met in practice - to ensure that checks and balances are included without questioning the technical positions taken. However we are of the opinion that if remedial action is taken in the due process by the IASB the DPOC should consider the causes of that action and the underlying decisions that had to be remedied.
57. In paragraph 2.5 of the introductory section it is stated that the oversight process will be conducted through transparent procedures and responding to issues raised. We believe, however, that the oversight should not only be reactive in nature and that the oversight section would be better guided by a more pro-active spirit. In our view global standard setting requires a pro-active oversight process restricted neither to review or a 'box-ticking' confirmative process nor to compliance/conformity testing. We believe that an active oversight process focusing more on the substance would also reduce incidents and problems that we raise in the following paragraphs. Furthermore we believe that the deliberations of the DPOC should be held in public and the results of the DPOC deliberations should be made publicly available.
58. We welcome that a function Director for Trustees' activities has been created. We believe this will bring to the DPOC the means in dedicated staff that it needs to lead its independent review. In addition, we do not believe that the DPOC should limit its oversight to raising questions to, and receiving answers from, those directly involved in the project: an independent review of the due process is needed. In this context, we do not believe it is appropriate that IASB staff is asked to respond to concerns raised on the due process of the standards in which they were involved. The IASB is responsible for issuing new accounting standards or interpretations. As a consequence, any concerns with respect to the way in which standards were developed, and how concerns raised by constituents were addressed and why the IASB did or did not take these concerns into account in finalising the standards, need to be answered by the by the DPOC, on the basis of analyses led independently by its dedicated staff, and after proper discussion and evaluation with the IASB. It is not appropriate for the staff

involved in the standards to assess whether the due process was respected. This is necessary to discharge the responsibility of the DPOC set out in paragraph 2.8 (d).

59. The consultation process on ED 9 on Joint Arrangements is an example of the limitations of current practice. Notwithstanding a substantial change in guidance in the final standard, the staff explained in the Project Summary and Feedback Statement that a re-exposure of the proposals was in their view not necessary. Yet the additional guidance is causing important implementation issues for a group of preparers which have not been able to react to this in the consultation process.
60. Paragraphs 8.5 and 8.6 indicate how the DPOC handles breaches in due process. We support the general thrust of those paragraphs. However paragraph 8.5 seems to suggest that a breach of due process can never lead to a pronouncement being invalid. We believe that this should be revised. Indeed retrospective remedies to the breach of due process may have to lead to suspend pronouncements if publication has taken place before the breach of due process has had a chance of being remedied, and a remedy is deemed necessary.
61. In addition, it would be helpful if it could be indicated in paragraph 2.8 (e) which committees are integral to due process (and which are not) and what the meaning of being integral to the due process is.
62. The level of oversight exercised by the DPOC as described in the areas of responsibility in paragraph 2.8 is different for different groups and processes, it is not clear to us why such a distinction is made.

**Question 2 - The DPOC have created a Due Process Protocol in the form of a table that shows the steps that the IASB must, or could, take, as well as reporting metrics to demonstrate the steps that they have taken, in meeting their due process obligations.**

**Do you agree with the idea that such a table should be maintained on the public website for each project? Why or why not?**

63. EFRAG supports the transparency of the process and we agree that public reporting is one of the crucial elements enabling the stakeholders to assess whether the IASB has met their due process obligations. We also agree that such Due Process Protocol tables should be maintained publicly (i.e. through the IFRS Foundation website) for each of the projects.
64. We note that the Due Process Protocol in Appendix 4 is not an integral part of the Due Process Handbook, and may be updated by the IASB and its staff, subject to the approval of the DPOC. We can accept this process since we would consider that the Due Process Protocol sets out internal working procedures. However, it is important that there is consistency between the Due Process Protocol and the Due Process Handbook at all times and at all stages of the standard setting process, although the former will be more detailed. One way to ensure consistency would be to make the protocols an integral part of the Due Process Handbook.
65. An example of inconsistency is the due process in relation to 'Three-yearly consultation on the IASB technical work programme' described in paragraphs 4.3 to 4.5 and its due process protocol provided on page 48: in paragraph 4.5 it says the IASB must keep the Trustees informed whereas the protocol speaks about formal consultation with the Trustees. Another example is that paragraphs 6.16, 6.34, 7.12 and 7.27 require that exposure drafts, changes to IFRS, draft interpretations and interpretations must be accompanied by a press release whereas the respective protocols indicate that this step is optional. A further example is that the quality assurance steps as presented in the Due Process Protocols should have the same emphasis in the Due Process Handbook throughout the standard setting process including the final standard, final interpretation and the maintenance. In our opinion the quality assurance as presented at present in the Due Process Protocols pays much more attention to issuing publications before the final standard or interpretation than in finalisation of the standard or interpretation. Quality assurance should be embedded in all stages of the Due Process Protocols.

**Question 3 - A research programme is described, which we expect will become the development base from which potential standards-level projects will be identified. In addition, a new section on maintenance has been added, which formalises the practice that the IASB and the Interpretations Committee have been following for addressing matters that are narrow in scope. It clarifies that the more formal project proposal processes were always intended to apply to new IFRSs and major amendments. The IASB has the discretion to initiate changes that are narrow in scope to IFRSs as part of the general maintenance of IFRSs. The new section also explains how the activities of the IASB and the Interpretations Committee are closely related.**

**Do you agree with the distinction between narrow-scope projects, which come under the heading of maintenance and comprehensive projects, which come under the heading of development of IFRSs? Why or why not?**

**Do you agree with the introduction of a separate research programme that will likely be the development base from which potential standards-level projects will be identified? Why or why not?**

66. We welcome the introduction of the research programme phase into the due process and we support the idea that research programme should precede an addition of a standards-level project to the IASB agenda. We are also appreciative that the Discussion Paper is brought to the research programme phase which meets our request for evidenced based agenda setting that we raised in our Comment Letter on the "IASB Agenda Consultation" of 5 December 2011. The research programme phase would include the public consultation on research papers and/or discussion papers before a specific project is added to the IASB technical programme as a standards-level project. We recognise that it is important that the research programme phase is undertaken in liaison with the academic community and other organisations that undertake or sponsor research (such as EFRAG in partnership with National Standard Setters in Europe).
67. We believe that it would be useful if the Due Process Handbook would address the main aspects of the management of the research programme phase including criteria when to finish a research programme phase and what to do if no reasonable results occur.
68. Paragraph 5.2 states that publishing a discussion paper before adding a standards-level project to the IASB technical work programme is not a requirement and proceeding without a discussion paper is possible. We believe that a research programme phase should always be concluded by a public consultation phase on the issue and the possible approaches considered to address the issue before deciding to add a project to the standard-setting programme. The findings and conclusions reached as a result of this public consultation on the discussion paper or research paper in relation to the decision on entering the standards level phase should be publicly available.

69. The need for improvement should clearly be demonstrated resulting in better financial reporting in practice, meeting the overall principle in the covering letter that improvement of financial reporting at reasonable cost should be the sole driver for changes to standards and interpretations. This is the way to achieve shared identification with constituents and hence paving a positive and collaborative process for change. This will have the supplementary merit of prioritising the IASB work programme on the basis of the needs of those who apply IFRS in practice. EFRAG believes that amendments to IFRS aiming at attracting potential new IFRS adopters should not be made at the expense of existing users of IFRS.
70. We agree that whether a discussion paper is needed or not depends on how fundamental the change is e.g. we think that a change in core principles should always be supported by a discussion paper, but for non-fundamental changes, issuing discussion papers may not be necessary. We would welcome the development of explicit criteria as part of the Due Process Handbook to guide these decisions.
71. As indicated above we welcome the inclusion of the discussion paper into the research programme phase. We also welcome that paragraph 6.5 states that developing an exposure draft normally begins with the IASB considering issues, including comments received on any discussion paper. We would like, however, to underline that the findings and results of the public consultation on discussion papers should always be taken into account when developing exposure drafts. All problems identified at discussion paper stage should be appropriately addressed. We refer in particular to the recent experience with the revenue recognition project where problems identified at the discussion paper phase in relation to impacts on certain industries were not or not sufficiently considered at exposure draft stage.
72. In our opinion the criteria for new IFRS or major improvements set out in paragraph 5.1 for the decision whether a proposed agenda item will address users' needs would benefit if they were developed further. More in particular it would be helpful to clarify how these criteria assist in the distinction between narrow-scope projects and new IFRS or major amendments.

**Question 4 - Two changes to comment periods are proposed. The first would increase the minimum comment period for exposing the draft of a rejection notice of a request for an Interpretation request from 30 days to 60 days. The other change relates to the re-exposure of a document. The DPOC is proposing to allow the IASB to have a reduced comment period of a minimum of 60 days for documents it plans to re-expose, if the re-exposure is narrow in focus.**

**Do you agree with the changes in the comment period lengths for rejection notices and re-exposure drafts? Why or why not?**

73. EFRAG supports the increase of the minimum comment period for a draft of the rejection notice from 30 to 60 days. However, we think that in case of controversial items, the 60 day term may not be enough for the regional and national accounting standards bodies and other participating organisations that proceed with their own due processes to respect consultation obligations with their stakeholders.

74. We can accept the DPOC's proposal to allow the IASB to have a reduced comment period of a minimum of 60 days for documents it plans to re-expose, if the re-exposure is narrow in focus. However, we believe that the Due Process Handbook should include criteria to assess when re-exposure is narrow in focus and thus minor and non-controversial and to guide its decision. Such criteria should in our view include: the magnitude of the change; the magnitude of past controversy of the former proposal; and the size of the potential impact in practice. If any one of these criteria is not met, the comment period should be at least 90 days.
75. In addition to the above reservation we have concerns about paragraphs 6.7, and 6.8 which address the length of comment period for exposure drafts. We do not support the possibility to shorten the comment period below 30 days. Although we note that according to the proposed Due Process Handbook this would only be applied in exceptional and urgent cases and be subject to approval of the DPOC or the Trustees, we would expect in all cases a minimal commenting period of at least 60 days to allow constituents to respect their own due process.
76. Furthermore, we are concerned that the 60 day comment period on a Request for Information is unreasonably short for the regional and national accounting standards bodies. Whilst we agree that IASB's due process must allow it to proceed on a timely and effective manner, it should be taken into account that regional and national accounting standards bodies need to respect their own due processes in order to fulfil their consultation obligations with their stakeholders. In general, a 60 days period is therefore too short. In particular, more complex issues that would require deep discussions and several meetings will not fit the 60 day period to conclude on the findings to be transmitted to the IASB. An example where, in our experience, a 60 day comment period was too short is the Supplementary Document with regard to Financial Instruments Impairment in January 2011: this did not allow sufficient time for outreach activities.
77. In our opinion the decision on the length of the comment period should take into consideration all the important factors that would affect the constituents' ability to prepare balanced comments whilst respecting the constituent's own due process. The typical closing periods, vacation periods or other relevant habits should be taken into consideration in order to meet the full and fair consultation principle. The comment period should allow sufficient time for all constituents to provide comments, and not necessarily be the minimum required comment period for the pronouncement concerned.

**Question 5 - Are there any other matters in the proposed handbook that you wish to comment on, including matters that are not covered by the handbook that you think should be?**

We refer to our comments in Appendix 1.