



Ms. Françoise Flores
Chair
EFRAG TEG
Square de Meeûs 35
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Ref.: FRP/PRJ/HOL/TSI/SRO

Dear Ms. Flores,

Re: FEE Comments on ASB and EFRAG Discussion Paper on Considering the Effects of Accounting Standards

- (1) FEE (the Federation of European Accountants) is pleased to comment on EFRAG's consultation on the effect of accounting standards. FEE commends EFRAG, the ASB and other European Standard Setters for issuing this discussion paper which in our view represent a valuable contribution to an important debate in regulation and standard setting.
- (2) FEE repeatedly advocated towards the IASB on the need to devote the necessary time and resources to assess the impact of any significant project that the Board undertakes. It is indeed very useful to provide views on when and how such effect studies should be performed.
- (3) We underline that effect analyses are not something entirely new, since they are already built into the current IASB due process. However, at present effects analyses are only formally undertaken at the level of exposure draft whereas EFRAG rightly puts the emphasis on gathering evidence of effects during the entire life-cycle of a project. We believe that acknowledging the fact that it is expanding existing processes rather than creating something entirely new aids to a better understanding of the contribution the EFRAG Discussion Paper is seeking to make.
- (4) The key points in our response are:
 - We agree that effects analyses should be embedded in the standard setting process throughout the life cycle of a project. We believe that a clearer distinction should be made between effects analysis ex ante and ex post, since we believe that post-implementation reviews are different from ex ante effects analyses.

- We believe that in particular at the stage where a decision is made to add a new project to the IASB agenda, there needs to be a clear problem definition of what issues a new project is seeking to address as well as evidence of the expected effects.
- Effects should include both micro-economic and macro-economic effects.
- FEE favours a process that is both pragmatic and robust. The IASB should be responsible for performing effect analysis, and the effort involved should be relevant and proportionate.
- For the effects analysis process to have genuine credibility, robust oversight by the Trustees' Due Process Oversight Committee (DPOC) is paramount at all stages of the process to mitigate any self-review risk. This risk is particularly high, either real or perceived, at the stage of post-implementation reviews and therefore warrants significant DPOC involvement.
- Finally, we point out that the discussion paper can be improved by eliminating some sections that seem repetitive or unnecessarily detailed. Our more detailed comments are included in the responses to the different questions raised by EFRAG.

We would be pleased to discuss any aspect of this letter you may wish to raise with us.

For further information on this letter, please contact Tibor Siska, Project Manager, at FEE Secretariat on +32 2 285 40 74 or via email at tibor.siska@fee.be.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Philip Johnson', with a long, sweeping horizontal stroke extending to the right.

Philip Johnson
President

Question 1 - Do you agree that “effects analysis” should be defined, for the purposes of accounting standard setting, as “a systematic process for considering the effects of accounting standards as those standards are developed and implemented” (paragraph 2.2)?

- (5) FEE agrees with this single definition. Although ex ante analysis will often necessarily be based on ex post studies pointing to loopholes in the set of standards or failures of standards, we believe that it is useful to distinguish between ex ante and post implementation effect analysis¹.
- (6) Ex ante analyses are important to instil a greater degree of transparency, efficiency and accountability in the standard setting process. Ex ante effect analyses will be part of a more general evaluation which additionally requires that all relevant options are considered and that appropriate consultation is undertaken². This is necessary to ensure that the standard setter (or at a later stage those who will have to endorse the standard in different jurisdictions) have the right information to take their decision. However this process has inherent limitations as it is trying to measure future consequences of a decision to be applied in different financial and economic environments and circumstances.
- (7) Post implementation analyses contribute to the review of the effectiveness of the standards and intend to identify some loopholes or weaknesses in the implementation of the standard, which could potentially require further adjustments. Obviously, the data on which a post implementation analysis is based are fully measurable. Such studies could perfectly use tools that are usually applied to academic research.

Question 2 - Do you agree that effects analysis should be integrated (or further embedded) into the standard setting due process (paragraph 2.7)? If not, why not?

- (8) The IASB Due Process Handbook contains already many elements that could be considered as part of an effect analysis including field visits, field test and cost/benefit analysis. However FEE strongly supports the proposal in the EFRAG Discussion Paper that effects analyses should be more formally integrated into the standard setting due process. This is especially true as far as the initial phase of agenda decision is concerned.
- (9) FEE agrees that considering the potential effect of a new standard should start as early as possible in the standard setting process. Otherwise there is a risk that the effect study becomes an ex post rationalisation of policy decisions made at the earlier stage. As explained above, we believe that different stages in the process should be distinguished, which are not clearly similar in nature and in their purpose. In that respect we also refer to section 5 of the Discussion Paper:

¹ Final Report of the Mandelkern Group on better regulation, 13 November 2001, p.11
http://ec.europa.eu/governance/better_regulation/documents/mandelkern_report.pdf; OECD (2009) “Regulatory Impact Analysis – a Tool for Policy Coherence” p.151.

² OECD (2008) “Building an Institutional Framework for Regulatory Impact Analysis (RIA): Guidance for Policy Makers” p.17 <http://www.oecd.org/dataoecd/44/15/40984990.pdf>; in particular Chapter 2. “Determinants of Quality in Regulatory Impact Analysis” p.50 – 60.

- a. The initial stage of an agenda decision to take a project on, where the effect analysis focuses on the reasons for changes and priorities in the allocation of resources (preliminary assessment).
- b. The ED phase and decision-making on a particular accounting model prior to approval of a standard. The effect analysis in this stage should:
 - Raise questions about the different possible options considered and discuss why an option has been preferred;
 - Gather evidence on the expected consequences of the different solutions at the level of individual companies and macro-economically as a result of the choices made;
 - Open a consultation of stakeholders.
- c. The post implementation review to consider how far intended consequences are effectively attained and also unintended consequences.

Question 3 - Do you agree that the standard setter should be responsible for performing effects analysis, and that the performance of effects analysis by any other body is not a sufficient or satisfactory substitute (paragraph 2.11)?

- (10) FEE agrees that the IASB should be responsible for performing effects analysis as the purpose of the process is to ensure that the standard setter is fully aware of the likely consequences of its decisions. The IASB due process handbook should recognise that effects analyses are part of a continuous process to inform the standard setter in its decision making. The Due Process Handbook should also stress that it is part of the trustees' due process oversight role to review the compliance with the requirements to carry out effect analyses in the various stages of the standard setting process.
- (11) At the post-implementation stage, the involvement of the Trustees' Due Process Oversight Committee is even more relevant to avoid the risk of self-review. The effect analysis at this stage should not be limited to a pure compliance exercise. It should also look at unintended consequences. While respecting the principle of proportionality, the trustees should consider whether the work should be carried out with involvement of third parties.

Question 4 - Do you agree that effects should be considered throughout the life-cycle of a project to introduce a new accounting standard or amendment, but that publication of a document setting out the key elements of the effects analysis should be specifically required, as a minimum, at the following points in time in that life-cycle (paragraph 2.15)?:

- A. When an agenda proposal on the project is considered by the standard setter;
- B. When a discussion paper is issued for public consultation (this effects analysis is an update to "A", to reflect the latest information available);
- C. When an exposure draft is issued for public consultation (this effects analysis is an update to "B", to reflect the latest information available);
- D. When a final standard or amendment is issued (this effects analysis is an update to "C", to reflect the latest information available); and
- E. For new accounting standards and major amendments, a "post implementation review" is required, which is an analysis of "actual effects" that should be performed and published when the pronouncement has been applied for at least 2 years, together with the publication of an associated document setting out the key elements of the review; a post-implementation review is not required for minor amendments.

- (12) FEE agrees that effects should be considered throughout the life-cycle of a project to introduce a new accounting standard or amendment. At a very early stage (see above para. 6.a), a preliminary assessment should identify the problems or risks to be addressed and the companies/industry or stakeholders which will be most likely affected in order to launch early external consultations. Such early assessment could also be helpful in considering the adequate depth of the analysis work (see question 5 and response).
- (13) FEE is not entirely convinced that a document setting out key elements of the analysis is useful at the level of the Discussion Paper. The purpose of the Discussion Paper is to disclose different options and to collect views from stakeholders, which in itself is part of the effect analysis. Therefore effect studies at this level would be broadly repetitive with a well understood discussion paper.
- (14) Furthermore in a number of cases, especially amendments to standards, phase A and E are likely to coincide. Similarly one can consider that the effect study attached to a draft standard should be the draft effect study which would be published with the final standard except for amendments that would be brought at this phase of the development of a standard.
- (15) Performing effect studies within a very short interval on a continuous basis could become very burdensome. Effect studies should not be carried out for the sake of doing it. It should remain relevant and proportionate.

Question 5 - Do you agree that effects analysis should be undertaken for all new accounting standards or amendments, but that the depth of the analysis work should be proportionate to the scale of the effects (in terms of their “likelihood” of occurring and the magnitude of the “consequences” if they do occur), the sensitivity of the proposals and the time available?

- (16) FEE agrees that effect studies should be undertaken for every new standards and amendments. However we very much support the views that it should not become an excessively bureaucratic exercise. It should proportionate to the scale of the likely effects and the sensitivity of the proposal. The experience of EC impact assessments shows that the implementation of the concept of proportionality requires attention³.
- (17) Conversely, except for very exceptional circumstances, we believe that time available should not play a role and become an easy excuse for lowering the quality of the study.

Question 6 - Do you agree that “effects” should be defined, for the purposes of accounting standard setting, as “consequences that flow, or are likely to flow, from an accounting standard, referenced against the objective of serving the public interest by contributing positively to delivering improved financial reporting” (paragraph 3.2)?

³ Renda Andrea “Impact Assessment in the EU” CEPS, Brussels, 2006 p.91.

- (18) As a general remark concerning section 3, we believe that the discussion paper would be improved by providing more practical examples. Other areas on which standard setting might have a side-effect to be considered could be identified or made more explicit with reference to practical situations.
- (19) FEE agrees with paragraph 3.2 of the Discussion Paper; see however our comments under question 10 addressing a similar issue.

Question 7 - Do you agree that the term “effects”, rather than the term “costs and benefits”, should be used to refer to the consequences of accounting standards, in order to distinguish effects analysis from a CBA, on the grounds that it would not be appropriate to require a CBA to be applied to standard setting (paragraph 3.7)?

- (20) FEE agrees with the proposal to use the word “effects” instead of “costs and benefits” because the measurement tools are not necessarily the same for costs and benefits so that it will often be difficult to match the two elements. It should be noted however that arguments in paragraph 3.10 are often heard by many people opposing CBA in other areas of regulation so that they are not necessarily specific to financial reporting standards.
- (21) The debate on quantitative effects versus non-quantitative/qualitative effects is difficult. Although quantification will often be more powerful, the objectives of the standard setter/regulator will normally be qualitative. We do agree with EFRAG that in certain circumstances, it will be appropriate to perform a quantitative assessment of costs and benefits as part of the process of competing effect analyses (paragraph 3.8). In any event, effect studies must be honest in considering all aspects of the proposal made. Effect analyses should assess advantages and disadvantages for the identified or affected companies and stakeholders.
- (22) Even though quantification is not the preferred method used for effect studies in the area of financial reporting standards, the IASB should specifically consider the cost element for smaller companies when discussing the possible options and the preferred solution in their assessment report.

Question 8 - Do you agree that the scope of the “effects” to be considered, for the purposes of performing effects analysis, should include all effects, both “micro-economic effects” and “macro-economic effects” (paragraph 3.12)?

- (23) FEE agrees that all effects both micro-economic and macro-economic must be considered. The difference between micro and macro-economic effects is not always very clear. For instance, the volatility of financial instruments on insurance plays a role at the level of an entity but it also has major consequences at the level of the insurance industry. Therefore, in economic regulation, such distinction is not always very relevant. FEE would not support however the counter-argument in paragraph 3.15 of the Discussion Paper.
- (24) Monitoring financial stability falls clearly outside the remit of the IASB. However, the standard setter should not ignore the effects that his decision might have in other areas. This is part of the reasons for having an impact analysis. It is especially useful to consult extensively with those in charge of the supervision of specific industries and to report on these consultations in the effects analysis.

- (25) More broadly, the consultation of stakeholders on discussion papers and exposure drafts is an important element in the evaluation of the likely consequences of a draft standard. Therefore, the effect studies should pay enough attention to highlighting the positions of stakeholders and especially ensure that responses can be collected from relevant interested groups of entities. On this specific aspect, FEE believes that the Trustees' Due Process Oversight Committee should ensure that IASB is giving enough time to stakeholders to analyse carefully possible effects of a draft standard.
- (26) Differences in the socio-economic characteristics of the different regions in the world make it constructive for any global standard setter to prepare its effects-analysis in close cooperation with regional organisations able to collect information on likely effects of a standard/ regulation in this region.
- (27) It is especially relevant for post-implementation reviews to verify that effects do not substantially differ from one region to another.

Question 9 - Do you agree that a standard setter can only be expected to respond to an effect which is outside of its remit (or for which an accounting standard is not the most effective means of addressing the particular effect) by communicating with the relevant regulator or government body to notify them of the relevant issue and to obtain confirmation from them that they will respond appropriately to it (paragraph 3.17)?

- (28) FEE agrees that a standard setter can only be expected to respond to an effect which is outside of its remit by communicating with competent organisations. Macro-economic consequences can be far-reaching. For instance evaluating accounting for pensions means that you will look at the structure of the population which will not be the same for instance in the EU or in India. One could ask whether IASB is best placed as an organisation to carry out such studies. Communicating with regulators or government bodies might be a solution in many cases but not always.

Question 10 - Do you agree that "effects" should be defined by reference to an objective, and that the objective should be that of "serving the public interest by contributing positively to delivering improved financial reporting", where "serving the public interest" means "taking into account the interests of investors, other participants in the world's capital markets and other users of financial information" (paragraph 3.19)?

- (29) FEE agrees that the reference to an objective will help clarifying the definition of effects. EFRAG's approach as discussed in paragraphs 3.20 and 3.21 is acceptable.
- (30) However FEE believes that the current text could be interpreted as meaning that as long as a positive contribution is made to improving financial reporting, the public interest consideration is, by default, met. We are not convinced that this is sufficient to justify action for instance where the costs are disproportionate.

Question 11 - Do you agree with the following clarifications of the term "effects"?:

- a) Effects can be "positive", "negative" or "neutral", as determined by whether they support, frustrate or have no impact on the achievement of the objective of serving the public interest by contributing positively to delivering improved financial reporting (paragraph 3.23);

b) *Effects analysis will usually involve assessing the “marginal effects” of an accounting standard or amendment, relative to the status quo that existed before its introduction, so the term “effects” should, in general, be interpreted to refer to “marginal effects” (paragraph 3.24);*

c) *The term “effects” can be used to refer to both “one-off effects” and “ongoing effects” (paragraph 3.26); and*

d) *The term “effects” can be used to refer to both “anticipated effects” and “actual effects”, depending on what stage the effects analysis is at – before, during or after implementation of the new accounting standard or amendment (paragraph 3.28).*

(31) FEE agrees with clarifications of the term “effect” in question 11.

Question 12 - Do you agree with the following further considerations concerning effects:

a) *Effects analysis should involve considering effects in terms of both their “incidence” (who is affected) and their “nature” (how they are affected), and that the standard setter should be transparent about whether and why they consider that the effects on one group should receive greater weight, less weight or equal weight to the effects on any other group (paragraph 3.30); and*

b) *Effects analysis should involve prioritising effects, possibly by “ranking” them in terms of their “likelihood” of occurring and the magnitude of the “consequences” if they do occur (paragraph 3.32).*

(32) FEE has no further comments on considerations concerning effects in question 12.

Question 13 - Do you agree that there should be a set of key principles underpinning effects analysis (paragraph 4.2)?

(33) Yes we agree with the need of key principles.

Question 14 - Do you agree that the set of key principles underpinning effects analysis should be as follows (paragraph 4.2)?:

Principle 1: Explain intended outcomes (refer to paragraph 4.2);

Principle 2: Encourage input on anticipated effects (refer to paragraph 4.2);

Principle 3: Gather evidence (refer to paragraph 4.2); and

Principle 4: Consider effects throughout the due process (refer to paragraph 4.2).

(34) FEE agrees with the set of key principles underpinning effects analysis as proposed in the Discussion Paper.

(35) FEE believes that principle 1, at the agenda-setting stage implies a clear statement of the problem or risk to be addressed and the reason why action is required.

(36) Principle 2 promotes rightly “active” encouragement to provide input. When it is clear that the proposed standard will have a bigger impact on identified groups of companies or other constituents, such active consultation is necessary while respecting the principle of transparency which is rightly emphasised in paragraph 4.5. The involvement of regional organisations in the consultation process should be further encouraged as explained above.

Question 15 - Do you agree that the process that a standard setter should apply for validating the intended outcomes of a proposed accounting standard or amendment should include steps “a” to “d” of paragraph 5.2?

- (37) FEE agrees with the process that a standard setter should apply for validating the intended outcomes of a proposed standard.
- (38) In our views, validating intended outcomes constitutes the preliminary assessment (the expression provisional analysis is used in paragraph 5.2) at the initial stage of an agenda decision, where the effect analysis focuses on the reasons for changes (see our answer to question 5). Therefore the Discussion paper should mention the proportionality test that should be carried out at this stage to conclude on the in depth analysis of the second phase. The first bullet point under 5.3.(a) should also be part of this preliminary assessment.
- (39) We very much support the proposal in paragraph 5.2.(c) that stakeholders be offered the possibility to react on the provisional analysis. After this consultation, it seems obvious that the standard setter should consider the answer before deciding to move forward with the next stage in the development of the standard.

Question 16 - Do you agree that the process that a standard setter should apply for identifying and assessing the effects of a proposed accounting standard or amendment should include steps “a” to “f” of paragraph 5.3?

- (40) The Discussion Paper proposes to identify and assess effects, before the identification of options and the selection of the preferred option. In this approach, the identification of options appears to be the conclusion in terms of standard setting/regulation of the main part of the effect analysis which would then be part B of section 5. However, when reading paragraph 5.3, it seems that several element of section B will be repeated in the analysis of the different options, which makes the process rather burdensome. For instance paragraph 5.3 (e) and 5.4 (e) refer to a public consultation. It should be recognised that paragraph 5.3 and 5.4 will normally be covered in the detailed effect analysis but they need not be separate parts in the report submitted to public consultation.

Question 17 - Do you agree that the process that a standard setter should apply for identifying options for the proposed accounting standard or amendment (options for achieving the intended outcomes of the proposed accounting standard or amendment), and for choosing the preferred option, should include steps “a” to “f” of paragraph 5.4?

- (41) Paragraph 5.4 (e) proposes a public consultation to validate the assumptions that the standard setter made. We suggest going further in the detailed effect studies. When different options are being considered, the standard setter should conduct a preliminary informal consultation with companies/industry or stakeholders which will be most likely affected and indicate their reaction related to these different solutions. This is most useful when a standard is especially relevant for a specific group of preparers or users.
- (42) As indicated above, we also believe that a consistency check between standards and also with the framework should be part of the analysis of the different options.

Question 18 - Do you agree that the IASB should, to some degree, delegate to national standard setters and similar institutions some of the activities involved in gathering evidence of the effects of accounting standards, particularly consultation with constituents, and that these bodies should play a more active part in the due process to ensure that IFRSs contribute positively to delivering improved financial reporting (paragraph 5.5)?

- (43) As explained above, detailed effect studies should analyse the likely consequences of a standard for companies/industry or stakeholders which will be most likely affected. Differences in the cultural and economic situations around world should encourage the global standard setter to consider the effects of its proposals in close cooperation with national standard setters and regional organisations which are best placed to collect information on likely effects of a standard/ regulation in their respective constituencies. We agree with EFRAG's proposal in paragraph 5.5.

Question 19 - Do you agree that the next steps in developing and, subject to the results of public consultation, implementing the proposals put forward in this paper should include steps "a" and "b" of paragraph 6.2?

- (44) We have no further comment on question 19.