What's Ahead for

Global Standards?

An interview with

Sir David Tweedie,

chairman of the International Accounting Standards Board

By Ramona Dzinkowski

What are some of the latest developments regarding standards setting in the global community? What other issues are affecting management accountants throughout the world? In this interview for *Strategic Finance*, Sir David Tweedie, chairman of the International Accounting Standards Board (IASB), offers a view on the global economic downturn and the relevance of International Financial Reporting Standards (IFRS) to restoring growth.

RD: One traditional argument for the global adoption of the International Financial Reporting Standards was that a common framework for financial reporting would increase the transparency and comparability of financial results between companies from different countries, thereby creating a level playing field for capital and, ultimately, improving capital mobility. How has the economic crisis underscored this argument, if at all?

SD: The view of the G20 and others is that a global crisis requires a global solution. IFRS are well advanced toward becoming the global language for financial reporting, which is one of the reasons why G20 leaders at their meeting in London this year called for substantial progress to be made toward global accounting standards. The effect of the downturn has been to emphasize the need for a single set of standards. Second, we really will be in trouble if we have two because, not surprisingly, if one set of banks feels that the other side is getting an advantage in a very specific area, they want exactly the same advantage. The opportunity for regulatory arbitrage is minimized when everyone is using the same set of standards.

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RD: Has the current economic crisis impacted the development of new global standards?

SD: It has led to a change in priorities in the sense that we have accelerated the replacement of the financial instrument standard. We would have done it in the next couple of years, so we will probably finish it now within 12 months.

RD: Have you seen a change at all in the progress of adoption of IFRS?

SD: It actually seems to have accelerated. Japan has permitted certain domestic companies to report under IFRS from this financial year. India has made a statement that it's going to go to IFRS in 2011. Korea is doing the same. So the big economies, especially in Asia, which were the last ones left of the big economies apart from the U.S., are now committing themselves to adopt.

RD: Some suggest that fair value [fair value accounting rules] is the culprit for creating this credit crisis. Can you comment on that?

SD: Fair value is not perfect, but much of the criticism of fair value has been a case of shooting the messenger. Its use in modern accounting has also been exaggerated. According to a study by the U.S. Securities & Exchange Commission (SEC) in December 2008, a minority of a bank's balance sheet is measured at fair value. Indeed, the Financial Crisis Advisory Group (FCAG), a body of senior leaders with broad experience with international financial markets, recently concluded that current accounting standards are likely to have underestimated the losses of financial assets. There have been some areas where we have had to make improvements, such as applying fair value in illiquid markets, but on the whole I believe that the enhanced transparency and comparability provided by fair value measurement is part of the solution, not the problem.

RD: What role does accounting have to play in restoring economic growth around the world? Do you see a direct link in the adoption of IFRS and the economic recovery?

SD: I don't think accounting is responsible for the crisis, nor is it going to get us out of it either. What it will do is bring everybody to a situation where you can understand what's going on in foreign companies as well as those in your own country. So what it does do is increase transparency worldwide, which is essential for investor confidence.

RD: How effective will the modifications to SFAS No. 166, SFAS No. 167 (which, beginning in January 2010, change the way banks and other financial institutions account for securitizations and special-purpose entities) be in increasing transparency of financial reporting in banks, and what should the role of the regulators be? [Statement of Financial Accounting Standards (SFAS) No. 166, "Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140," and SFAS No. 167, "Amendments to FASB Interpretation No. 46R," have been superseded by FASB Accounting Standards Codification™ Topic 105, Generally Accepted Accounting Principles.]

SD: It's an important step for the U.S. as it will bring assets back on the balance sheet that perhaps should have been there in the first place. From what I gather, it's not so much that the standard was defective—it was the way it was applied that was defective.

RD: Lately there's been some concern that the U.S. has lost interest in adopting IFRS for the foreseeable future. In your view, has the economic downturn permanently forestalled the adoption of IFRS in America?

SD: I don't believe so. Policymakers have been pretty busy during the last year or two managing the response to the crisis. The U.S. is no exception, and it is no surprise if discussions regarding IFRS have slipped. That said, the G20 and others see the need for global standards as an important lesson of the crisis, and we continue to work with the FASB toward the goal of having substantially similar standards in place by 2011. The drivers for global accounting standards have not gone away as a result of the crisis. In fact, they have become stronger.

RD: Do you see the SEC supporting IFRS adoption again?

SD: Chair Mary Schapiro and Chief Accountant James Kroeker have both said recently that the SEC plans to give further consideration to U.S. adoption of IFRS in the fall. The SEC has been a big supporter of global standards right from the outset. The new administration has come in and quite rightly wants to form its own views on a range of issues. But in all of our dealings with Mary Schapiro and her team, we have had nothing but support for our work and the project for convergence of IFRS and U.S. GAAP. Chair Schapiro said recently that it would be ideal to have a single set of high-quality accounting standards that work globally.

The proposed roadmap sets 2011 as the date that the

U.S. should decide on adoption of IFRS, so there is no urgency for a decision. The SEC also has a number of other issues on its plate right now.

RD: With the nature of the rules-based system in the U.S. and the quantity of U.S. GAAP and guidance, do you see any impasses to converging IFRS and U.S. GAAP?

SD: Yes. The rest of the world doesn't want 17,000 pages of standards. I think the only way for the U.S. to change is to switch to IFRS. You just can't get convergence of 17,000 pages with 2,500. It would take years and years.

RD: Under what circumstances do you see that the U.S. issuers will accept a principles-based approach with little or no guidance? I'm curious if that world exists out there.

SD: Well, the IASB does have guidance, but what we're trying to do is minimize it. Our view is if you'd like us to deal with 80% of the issues, we can do that in 30 or 40 pages. If you want us to deal with 95% of the issues, you're up to 300. And the extra effort for the 15% is just frankly not worth it. Now the rest of the world is quite happy with that. Interestingly, we were always told that, when Europe changed, the IASB would be deluged with questions. We weren't. Our interpretation committee last year issued three interpretations. The EITF [Emerging Issues Task Force of the FASB] in America tends to issue about 20 a year—and all for a single economy—yet the rest of the world manages with three or four. So, there's not a demand really. I remember watching a U.S. litigation lawyer. He held up a copy of the American Constitution in one hand and with difficulty lifted the American standards on financial instruments in the other. And he asked, "Which do you think I'd prefer to defend in court?" He said, "I can defend a principle, but when you miss something on page 1,741, you're dead."

RD: The engine for global economic growth, at the current time anyway, is Asia. Many of these economies have significantly different business and legal environments from those operating in Europe or North America. Can you talk to some of the unique reporting issues in those economies?

SD: There aren't as many as you'd think. One of the things we always do when a country says it would like to change to IFRS is first to work out the differences between their local reporting standards and our standards. If they believe the IFRS is superior to the local standard, we expect them to adopt the IFRS. Second, we ask if they have to change their laws to fit in with the international community. Third, if they think they have a better standard, we will go and look at it. If it's appreciably better than the IFRS, then we will adopt it. And fourth, we'll ask if there's a situation that they have that's quite unique.

Now, we've only found two things so far. One was in China. If you're going to deal with related parties and the state is the related party all the way through, you'll end up with pages and pages of meaningless notes. So we had to put in something saying that if you're in a former state-controlled economy, then you'll just have to say what sort of dealings you're having with other companies that are run by the government as well. It puts everyone on alert that this company earns a large proportion of its income from dealing with other government companies. The second was what we've found in certain sectors in India and Korea related to foreign currency operations. Our existing standard doesn't work very well for them, so we've asked them to look at it and come back with solutions.

RD: The last question speaks to Europe. Have there been any significant issues with respect to adopting IFRS in Europe? Another point to that is what has the response been to the IFRS for SMEs [small and medium-sized entities]?

SD: Across Europe as a whole, the experience of moving to IFRS has been a positive one. In 2005, almost 8,000 listed companies in 25 countries moved from local GAAP to IFRS. An astounding feat. If the U.S. also decides to adopt IFRS, it will benefit from many years of convergence of U.S. GAAP and IFRS, so the difficulties of transition, whilst challenging, should not be overstated. Regarding SMEs, the British are proposing to adopt it, and it's going very well in other parts of Europe. That standard is proving hugely popular. We reckon there will be millions of companies using it before long worldwide. A number of developing economies are already making plans to adopt it. There are only 250 pages, and it [the standard] deals with all the major issues that they have to deal with. **SF**

Ramona Dzinkowski is a Canadian economist and business writer living in Toronto. She is also executive director of the Canadian Financial Executives Research Foundation, the research institute of Financial Executives International (FEI) Canada. You can reach her at rndresearch@interhop.net.