



26 July 2011

Our ref: ICAEW Rep 75/11

Your ref:

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Dear Ms Murphy

EXPLORING A POSSIBLE METHOD OF INCORPORATION

ICAEW welcomes the opportunity to comment on the staff paper *Exploring a Possible Method of Incorporation*, published by the SEC in May 2011.

ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. As a world leading professional accountancy body, we provide leadership and practical support to over 137,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are a founding member of the Global Accounting Alliance, which has over 775,000 members worldwide.

ICAEW believes strongly in the benefits to investors and business of truly international standards, and has been a persistent champion of the creation of a single set of high quality global accounting standards and their application by publicly traded and other companies around the world. We made a significant contribution to the successful adoption of IFRS by UK listed companies in 2005, and our expertise in this area was reflected in the selection of the Institute by the European Commission (EC) to deliver a comprehensive study in 2007 covering all aspects of first time application of IFRS by European Union (EU) member states. In 2008 the Institute was also commissioned by the United Nations to prepare a follow-up report on the UK experience of IFRS implementation, which was presented in Geneva in October 2008. These reports and the extensive experience of our members in IFRS reporting have informed our comments on the staff paper.

‘Condorsement’

We understand fully the importance of exploring all of the options available to the SEC as it considers a radical change in the U.S. financial reporting regime. However, our experience of IFRS adoption in the UK and the rest of Europe leads to severe doubts about the solution proposed in the staff paper for moving the U.S. towards IFRS reporting.

When companies listed on the major EU regulated exchanges moved over to IFRS in 2005, transition was made on a mandatory, well-publicised and certain date. Our report to the EC on the transition, based on extensive reviews and research, concluded that the process was challenging, but successful, involving little if any market disruption and a generally positive outcome for companies, investors and other financial reporting stakeholders. The EU experience of simultaneous transition provided certainty, well-understood deadlines, and a clear focus and sense of purpose, enabling all participants in the process to share concerns and possible solutions. We have no reason to doubt, and there is no evidence to suggest, that the U.S. profession and other stakeholders would cope just as well with the transition in such circumstances. Simultaneous transition in Europe may also have facilitated a more efficient and cost-effective approach to IFRS training and learning for companies, auditors and users.

We would also highlight the more recent experience of converging the UK accounting standards applicable to private companies with IFRS. Much time and effort over several years was expended in bringing individual standards in line with IFRS before it became clear that completing the process was impractical. The outcome is a UK GAAP that no longer represents a coherent accounting framework, and does not sit comfortably alongside the parallel IFRS accounting regime. All of this work is now likely to be abandoned in favour of simple adoption on a single date of the IFRS for SMEs (with a few local adjustments).

We thus strongly recommend a simultaneous transition rather than a staged one, at least for major corporations (with foreign registrants able, as now, to file IFRS financial statements without reconciliation). The market is better able to deal with a single, well-understood change rather than a complex and protracted process of change. We recognise that there are important benefits to some element of phasing for smaller companies, which tend to have fewer resources available. But the endorsement approach seems to us to be fraught with risks and drawbacks, for both investors and preparers. The disadvantages of the proposed model are well articulated on pages 20-23 of the consultation paper and we urge the Commission to give them full consideration. We would only add that, while the period of transition is estimated to extend for five to seven years - a period long enough to introduce enormous uncertainty for preparers and users alike - this appears unduly optimistic, given the complexity of the exercise and the continued evolution of IFRS over this period. We think the process as laid out in this paper might more realistically take some 20 years or more.

Finally, in this context, we would point out that the prospective application envisaged in the staff paper would not comply with the requirements of IFRS 1 on first time application of IFRS, and would lead to further divergence between IFRS and U.S. GAAP reporters, significantly impairing comparability. This would be particularly damaging to investor protection as the differences would be complicated for users to understand – aspects of financial statements being compared might be based on application of the same standard, but application in quite different ways.

Endorsement

We understand fully the SEC's inclination to consider the establishment of an endorsement process. We anticipate that the extensive and ongoing work undertaken to align IFRS and U.S. GAAP will mean that in most cases this will be a formality on the initial adoption of IFRS. We would sound a note of caution here, however, as experience of standard by standard endorsement in the European Union has highlighted a number of drawbacks.

Firstly, the process raises the opportunity for a two-tier IFRS to develop, with the potential for the standards in force in the EU to be out of line with those in other IFRS jurisdictions. At present, for example, IFRS 9 *Financial Instruments* has not been endorsed and therefore cannot be applied in Europe. Comparability is impaired by this approach.

Secondly, in Europe the protracted and multi-stage endorsement process has added a significant degree of confusion for users and preparers.

We would therefore recommend that the Commission seeks to establish from the outset a process that is as streamlined and as efficient as possible.

The FASB and SEC in an IFRS world

We welcome the clarity the paper brings to the future role of the FASB. We agree that the FASB will still have a valuable role to play after the move to IFRS and agree with the points made on page 9 of the paper in this regard. In general terms we believe the IFRS model is enhanced by engagement with strong national standard setters in each jurisdiction that has adopted IFRS. Those standard setters are in a position to contribute to and influence the work of the IASB, not least by gathering views of their own constituents in an efficient manner. We also believe that the transition to IFRS will not in any sense diminish the influence of the SEC over accounting standard setting. The United States is the world's largest economy and is home to its biggest capital markets, and can expect commensurate influence within the international standard setting institutions.

Indeed, we would urge the SEC to deploy its expertise and experience in regulating financial markets in the cause of a single global accounting language, to show leadership to the world at this time of economic uncertainty by steering the United States firmly on a course towards mandatory application of IFRS. As more and more countries move towards IFRS reporting, and seek to influence the development of the standards, it is highly desirable that the United States remains at the heart of the IFRS world. This is an historic, possibly unique, opportunity, and clear leadership at this juncture from the SEC and a strong and ongoing U.S. involvement in the IFRS standard setting process is likely to transform the global financial reporting environment, bringing substantial long-term benefits to investors and society generally, not only in the U.S., but around the world.

We are pleased to have been able to provide evidence and views to the SEC over a number of years, and are grateful for the contribution of SEC staff to our study for the European Commission in 2007. We would be delighted to offer further evidence to the Commission in its deliberations on the future of the Roadmap and the practical implications of IFRS transition.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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