What the future holds for international financial reporting

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Speaker: Hans Hoogervorst, Chairman, International Accounting Standards Board

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Introduction

One of the benefits of being Chairman of the International Accounting Standards Board (IASB) is that I get to spend time in some pretty amazing places. Mexico is one of those places.

When studying for my Masters' degree I majored in Latin American studies, so visiting Mexico has always been a pleasure and never a chore.

Of course, Mexico is far more than a destination for tourists. With Free Trade Agreements with more than 40 countries, Mexico is one of the most open countries in the world to international trade. As an export-oriented economy, Mexico has benefited hugely from globalisation. Mexico has become the destination of choice for multinational companies looking to tap into a business-friendly environment, with a highly skilled workforce.

Being fully wired into the global economy, Mexico' s decision to adopt International Financial Reporting Standards (IFRSs) in full from 2012 for listed companies made perfect sense. Business is more efficient when recognised industry standards are adopted. The same is true of financial reporting. By adopting IFRSs in full and without modification, Mexico will become fully compliant with financial reporting norms used by more than 100 countries, including two-thirds of G20 members.

From this year, international investors will be entirely familiar with Mexican financial statements.

A great deal of the credit for these achievements must go to the Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera, or CINIF The CINIF is an important partner to the IASB and we appreciate greatly your continued support.

Let us now move on to the business of the day.

As you may know, the IASB is approaching the completion of its convergence programme with the US Financial Accounting Standards Board (FASB). It is ten years since the boards set out on this path, and a great deal has been achieved. We have four remaining convergence projects to complete and I am hopeful that we can complete this work in relatively short order. Amaro Gomes, my friend and fellow Board member will provide you with an update on these projects later in the programme.

So, what then? What do the next few years look like for the IASB? What will our priorities be, and how should we use the limited resources at our disposal?

In the last year or so, the IASB, as well as our Trustees, have been giving serious consideration to these questions. The Trustees have recently completed their strategy review and the IASB is nearing the completion of its first comprehensive review of its future work plan.

If you want to know what the future holds for international financial reporting, there is no better place to look than these two reviews. That is why I will spend the remainder of this talk describing what I believe are their most important elements.

Agenda consultation

Let us begin with the agenda consultation.

Sir David Tweedie, my predecessor as Chairman of the IASB, often used to say that the IASB had little control over its agenda.

This certainly used to be the case. The IASB spent its first five years improving IFRSs in time for adoption by Europe and other countries. The following five years were largely dominated by its convergence work with the FASB. Both of these events have delivered substantial improvements to the quality of financial reporting but they also predetermined the IASB's work programme.

This work is largely now behind us. For the first time in the history of the IASB, we will have a relatively clean slate. I say 'relatively', because the IASB has a constitutional commitment to complete post-implementation reviews two years after each new IFRS or major amendment has been implemented. Doing these reviews properly, and on a timely basis, will take up some time and resources of the Board.

Everything else is up for grabs. That is why the IASB has conducted a thorough and comprehensive consultation on its future agenda. In 2011 we published for public comment a consultation document that set out some ideas, but more importantly solicited feedback on the agenda. In parallel, the Board and staff have held numerous meetings, round-table discussions, webcasts and other outreach activities. For instance, a discussion forum will take place here in Mexico City next Friday at the Mexican Institute of Public Accountants.

We have made a particular effort to seek the views of the worldwide investor community.

We all know how difficult it can be to encourage investors to comment on a particular feature of an accounting standard that may not come into effect for another five years.

Undeterred, we held meetings with buy and sell-side analysts, heads of research and fund managers across the world. We held international webcasts and conducted online surveys with investor representative groups such as the CFA Institute.

I am pleased to say that as a direct result of this work we received more investor feedback on the agenda consultation than on any other IASB activity to date.

The consultation is ongoing, and while I do not want to prejudge the outcome there are some common themes that are easy to spot.

The most common feedback is a request for a period of stability. This is quite understandable. Ten years ago no major economies used IFRSs. Now, more than 100 do. At the same time, many of our standards have been re-written. That is ten years of unprecedented change. It is not surprising that our friends around the world want some time for the dust to settle.

Now we have most of the world on board, even a small change to a standard can be like dropping a pebble into still water. The changes will ripple-out and affect tens of thousands of preparers. Investors must become familiar with the new rules. Auditors must learn how to audit them and regulators will need to enforce them.

It's not just the final standard that must be digested. Every call for feedback on our proposals, in the form of discussion papers, exposure drafts and so on must be considered and in many cases responded to.

This is a responsibility that we take very seriously. That is why determining the IASB's future work programme will involve cherry-picking the most important areas where change is required. Let's fix what needs fixing, and no more. So what does that mean for our post-convergence work programme? Well, many of these areas fall naturally out of the feedback from the consultation.

First, there is almost universal support for completing revisions to our conceptual framework. This framework serves as a point of reference for the IASB's decision-making. Where choices are not clear-cut, the framework serves to encourage the IASB to make decisions that are consistent across the standards.

The framework is also an important reference for companies when applying principle-based standards. We already have a framework that works reasonably well. However, feedback from the consultation indicates that we should prioritise the completion of this work. Areas such as Measurement are just too important to ignore.

Second, it has become increasingly clear that we are suffering from disclosure overload. This is not entirely due to financial reporting. The plain fact is that businesses have become more complex. It is the job of financial reporting to describe this complexity, not to mask it.

Not all disclosures provide useful information to investors. Standard boilerplate responses are more about ticking boxes than helping investors really understand what is going on under the hood of the business. This is an issue that preparers, auditors, regulators and standard-setters will have to tackle together.

For our part, we need to make sure that disclosure requirements are appropriate. Bottom up; each individual disclosure requirement may have made sense when the standard was first introduced.

However, from a top-down perspective do the disclosures in totality improve the clarity of financial reporting, or do they make it more difficult to really see what is going on?

I suspect that there will be few quick wins. One investor's disclosure clutter is another investor's golden nugget of information. Taking information away is never easy. Nevertheless, feedback from the agenda consultation indicates that this is an important area for many respondents – particularly smaller listed companies, many of whom believe that the disclosure overload falls disproportionately on their shoulders.

Thankfully, we are not starting from scratch and some excellent preparatory work has already been completed in this area.

The Scottish and New Zealand accounting institutes, the French Autorité des Normes Comptables, the European Financial Reporting Advisory Group (EFRAG), the UK Financial Reporting Council (FRC) and the FASB have all conducted independent research on current disclosure requirements. We will continue to work closely with them and with other colleagues as part of a project to develop a new IFRS disclosure framework.

Next, we must decide what to do with Other Comprehensive Income (OCI).

OCI is increasingly used as a home for income of a less than certain nature. It is true that income reported in OCI should come with a health warning, yet investors ignore OCI at their peril.

Providing a clearer conceptual definition of OCI will help to address the endless debates about volatility and financial reporting, as well as tackling the thorny issue of recycling. There are no easy or clear answers, but this is a project that I am very much looking forward to getting my teeth in to.

Finally, there are a few other, less ambitious projects that the Board may well consider taking on. These include agriculture, business combinations under common control, hyperinflation and rate-regulated industries.

We have a few further round-table discussions planned, but I think it is fair to say that our direction of travel is becoming clear.

I am not ruling out other projects for consideration by the IASB, but if we are to provide a period of relative calm then difficult choices will have to be made.

Strategy review

This brings me on to the Trustees' strategy review.

As you may know, the Trustees have recently concluded a far-reaching review of the strategy and vision of the organisation.

The review was conducted in parallel with a separate governance review by the IFRS Foundation Monitoring Board, which oversees the work of the Trustees. Both reviews are well worth reading.

In their report, the Trustees made a number of excellent recommendations.

These include improvements to oversight of the IASB's due process and the establishment of a dedicated research function.

However, I believe the most important recommendation was the need for the IASB to strengthen and formalise its relationships with standard-setters, regulators and the accounting profession.

The development of IFRSs involves close cooperation with national and regional standard-setting bodies. Once issued, the standards are endorsed for use in jurisdictions around the world. Auditors then attest compliance with the standards while securities regulators enforce their use.

Up until now we have achieved great things through informal dialogue with other participants in this supply chain. However, it is now time to move from this loose affiliation to a more integrated supply chain based on strengthened and more formalised relationships.

An integrated supply chain means that you are better able to guarantee the quality of the product.

I see two important benefits to this work.

First, the formalisation of this network will greatly assist our global standard-setting activities by binding-in national and regional standard-setting bodies more closely and earlier on in the standard-setting process.

Doing so will allow the IASB, in a more inclusive way, to share the 'heavy lifting' involved in research, field testing and outreach activities. It will allow the IASB to tap-in to a broader pool of talent when considering difficult issues. It will also provide a more formal mechanism for this input to feed into our standard-setting process.

This network has the potential to improve the quality of the standards, to reduce duplication of effort between the IASB and other standard-setting bodies and to reduce the risk of non-endorsement of a particular standard.

That is why the formation of the Group of Latin American Standard-Setters, or GLASS, is so important to the IASB. The GLASS has the potential to provide a regional forum for national authorities to exchange views. We are very keen for this initiative to be a success.

Second, the network will provide a mechanism for all participants in this financial reporting supply chain to work together to encourage greater consistency in the implementation of IFRSs.

A single set of standards provides the baseline. However, the standards need to be endorsed, implemented, audited and enforced on a globally consistent basis. This network will provide a forum for securities and audit regulators, the profession and the IASB to discuss ways to improve consistency, and to address areas of divergence.

In many ways, this is the missing piece of the jigsaw of global accounting standards.
The construction of such a network is not without its challenges.

What should the membership criteria be? Most people understand what we mean when we referring to 'national accounting standard-setters'.

Yet, such organisations look very different in different countries. Some, like the FASB or the CINIF, are fully independent boards while others are an extension of the Ministry of Finance or the Central Bank.

How do we balance input from national standard-setting bodies such as CINIF and regional standard-setting bodies such as GLASS? What about organisations such as EFRAG, which is not a standard-setter but which obviously plays an important role in endorsement of IFRSs in Europe?

How should the network interface to the IASB? Should it be in the form of a technical advisory council, structured along similar lines to the existing IFRS Advisory Council or do we need to create some other mechanism?

These are challenges that we will begin to work through in the coming months. However, I am convinced that establishing this fully integrated supply chain of financial reporting is essential if the promise of global financial reporting standards is to be achieved.

Conclusion

Ladies and gentlemen, I am grateful for your attention. We have important work to do, and Mexico's support, as the current Chair of the G20, is very important to us.

I have shared with you today what I believe are the most important objectives and challenges for the IASB in the coming years. Our future agenda is becoming clearer. I fully expect that forging closer and stronger links between members of the financial reporting supply chain will help us to deliver high quality and more globally consistent standards of financial reporting.

Thank you for your time. I wish you a very successful conference.