

EUROPEAN OUTREACH ON THE IASB'S AGENDA CONSULTATION 2011

DASB

EFRAG

AMSTERDAM – 2 NOVEMBER 2011

PANEL

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- Philippe Danjou - *IASB member*
- Hans de Munnik - *DASB Chairman*

PREPARATION OF THE FEEDBACK STATEMENT

This note has been prepared for the convenience of European constituents by the EFRAG secretariat. It has been reviewed by representatives of the IASB and has been jointly approved for publication by representatives of EFRAG and the DASB attending the event.

Introduction

In July 2011 the IASB published its Agenda Consultation 2011. In this request for views, the IASB asks for constituents' views on the strategic balance and direction and specific projects to be included on its agenda. EFRAG published its draft comment letter in response to the consultation in August 2011. In addition, EFRAG, in co-operation with National Standard Setters, arranged a series of outreach events to obtain input from European constituents and to understand their main priorities and needs.

This feedback statement summarises the comments made at the outreach event arranged in co-operation with the Dutch Accounting Standards Board (DASB) on 2 November 2011 in Amsterdam.

The discussion focused on the issues related to:

- Agenda setting process
 - IASB's broad strategic direction
 - Evidence based agenda setting process
 - Research activities
 - Convergence
 - Request for a period of calm
 - Enhancement of the Conceptual Framework
- Specific projects to be included on the IASB's agenda
 - The role of EFRAG proactive projects
 - Projects suggested by participants
 - Interaction with other initiatives
- Other issues

Agenda setting process

IASB's broad strategic direction

The IASB's agenda consultation document (hereafter referred to as the 'IASB's Request') asks constituents what the IASB's strategic priorities should be, and how the IASB should balance these over the next three years. The IASB member present at the event highlighted the importance of European constituents' views to shape the IASB's broad strategic direction.

The IASB's Request identifies five strategic areas and groups them into two categories: developing financial reporting and maintaining existing IFRS standards.

At the event, the DASB Chairman expressed the view that a two-phased approach would be more appropriate in setting the IASB work plan. The first phase should be a conceptual approach, including a fundamental reflection on the following four key issues: (i) the boundaries of the IASB work; (ii) the finalisation of the Conceptual Framework; (iii) the need for industry-based standards; and (iv) the IFRS accessibility, in the sense that standards could be reorganised and reworded to make their application and understanding easier for preparers and users. The second phase should focus on the selection of projects. He also raised the question of how the agenda consultation and decision making interacts with the governance review of the Trustees and the Monitoring Board.

Regarding the boundaries of the IASB work, the IASB member noted that the Conceptual Framework, as currently drafted, defines the activities of the Board and limits its responsibilities to general purpose financial statements. He indicated that some felt that the IFRS practice statement on management commentary was beyond the remit of the IASB. This implies also that, for example, financial reporting by not-for-profit entities is out of the scope. So far, the IASB has not been asked to explore other sectors. However, the IASB is open to consider any recommendation derived from constituents' comment letters on this matter. He thought it was a misperception when some jurisdictions claim that the IASB only reacts to specific demands. The IASB's Request proved the opposite; it is an open and transparent process aimed at understanding the needs of investors, users, companies and other interested parties.

The IASB member agreed with the need to finalise the Conceptual Framework. However, he did not support industry-based standards. He underlined that entities (e.g. insurance companies) could carry out different types of activities, and it would therefore be more beneficial to develop standards for specific activities (e.g. insurance contracts) rather than for particular industries (e.g. insurance companies). In addition, as investors want to perform comparisons across industries, consistent accounting is needed for similar activities.

On the accessibility, the IASB member considered that focusing on activities rather than industries enhanced the accessibility of IFRS. However, he agreed on the idea of simplifying IFRS and making them more user-friendly. At a previous administrative session, where the need for simplification was discussed, it had been expressed that the content of IFRS was generally considered sound by preparers. However, middle sized listed companies need to rely on external accounting firms to understand IFRS. These companies cannot afford an internal department to monitor IFRS and find IFRS costly to apply. The convergence process between IFRS and US GAAP might have led to longer and more complex standards than initially intended by the IASB. The IASB member suggested a reorganisation of the standards by topic as a possible way to address this situation. In fact, he noted that this approach was already underlying some of the last initiatives taken by the Board; for example in the Leases project.

Regarding the suggested idea of a two-step process, the IASB member noted that he would inform the other IASB members about this view. However, he could foresee some practical

difficulties by applying the suggested approach. Several countries are currently moving towards adoption of IFRS and other countries intend to adopt or adapt them in the short or medium term. If the IASB focused strictly on fundamental discussions, there would be a risk of leaving their needs unattended.

A participant from an audit firm also commented on the two-step approach. From his point of view, a three year cycle would be too short to accommodate all the proposals suggested by the DASB Chairman. The participant highlighted that a fundamental reflection cannot be done every three years and suggested to reconsider the frequency. In relation to industry-based standards, the participant believed that it would be much better trying to find the roots of common matters, for example instead of discussed rate regulated entities and extractive industries to address intangibles. He called for a proper coordination between the individual standards and the Conceptual Framework.

A participant from an employer's organisation agreed on the request related to accessibility of IFRS: standards should be written in a manner that would make them easier to understand.

Evidence based agenda setting process

In its draft comment letter, EFRAG states that agenda decisions should be based on an assessment of the existing IFRS practice against the evolving needs for improved financial reporting. When there is evidence that a new standard, or amendment to an existing standard, is needed, the next step should be to develop a specified project proposal. Possible evidence may include a gap in the existing IFRS requirements, situations where information becomes less relevant or may be a result of post-implementation reviews.

EFRAG suggests in its comment letter that the project proposals should specify the evidence of the need for the new standard or amendment as well as its objective and scope in order to, at a later stage, be able to assess whether the application results in high quality and improved information. The project proposals should be subject to public consultation.

At the event, the EFRAG PRC / Supervisory Board member emphasised that the process was aimed to be based on evidence gathered from practice. In addition, he stressed that EFRAG believes that the project proposals should be subject to public consultation before a project would be started. This would ensure that the needs were addressed and the specific facts of the project would be well understood and supported by constituents.

The DASB Chairman questions the need for public consultation on project proposals when sufficient and compelling evidence already exists at agenda setting stage. The DASB Chairman wondered why constituents should be asked for their views on project proposals since this would take away resources from other projects. He also asked who would be responsible for collecting the evidence. He believed that the real issue at stake is which projects should get priority.

The IASB member noted that what was compelling in one jurisdiction was often not an issue in others and vice versa. In addition, users and preparers could have different points of view regarding future priorities. This is for example observed in relation to the business combinations

under common control issue. Some people believed it was important to deal with this type of transactions, while others were not concerned about the accounting treatment of such transactions. It is therefore difficult for the IASB to decide on whether to deal with the issue or not. In relation to the gathering of evidence, the IASB member pointed out that certain projects were added to the agenda based on particular concerns either of the Board members or the IASB staff, rather than as a result of specific external demands.

The EFRAG PRC / Supervisory Board member explained that EFRAG's initial thought is that it is beneficial to base the agenda setting process on evidence, which could be obtained directly from the post-implementation reviews or gathered on other ways from the IFRS community. It seemed that in the past the scope of some projects has been changed during its drafting stage, suggesting that projects may not initially have been scoped well. EFRAG thought that project proposals should describe the granularity of the issue to be considered, the type of output (review, improvement, amendment or new standard), the estimated time table, and other facts that would help staying focused on addressing the issue which led to project.

A participant from an employer's organisation believed that some criteria were necessary to define 'evidence' and when to take on board a new project ('recognition criteria'). He also noted that some specific economic activities were scoped out from the Conceptual Framework, and should not be included in the agenda setting process.

Another participant from an audit firm agreed with EFRAG's proposals. However, he doubted whether the process should be called 'evidence based' as he thought it was difficult to describe the meaning of 'evidence based'. He stressed the importance of effects studies as well as effect assessments and outreach activities before undertaking any project. The participant also suggested that the IASB should pursue a procedure to eliminate projects from the agenda ('derecognition criteria'). The IASB member agreed with this.

Research activities

The IASB's Request argues that investing time and effort in research activities could lead to more efficient standard-setting. At the event, the IASB member noted that the IFRS Foundation Trustees supported the idea of expanding research activities in their strategy review.

In its draft comment letter, EFRAG states that assessing changes in the current economic context and business reality will involve some research in particular in the area of corporate reporting. However, EFRAG believes that the IASB should make proper use of (existing) research in liaison with the academic community and other organisations that undertake or sponsor research but not allocate more resources than necessary to monitor developments that may influence financial reporting.

At the event, a participant from the EFRAG Secretariat noted that timeframes of academic research and of the standard setting process might be different. In particular for 'new' research it needs to be considered how to align pace of research with the pace of standard setting. A participant from EFRAG TEG added that in cases where the IASB wanted to outsource research, it should provide specific guidance on the aspects that needed to be addressed. If the research

activities were already carried out, he believed that adding some additional aspects would be straightforward. He underlined that research can help in finding the effects of standards.

The DASB Chairman noted that the issue of having research activities related to a particular issue is usually well understood, whereas the call for research in itself seems to trouble participants.

The IASB member stressed that the limits and effectiveness of research activities should be understood and its practical implications considered. In general terms, research is a slow process, but he still believed that some conceptual reflections should be based on research although a balance needs to be struck with practicality.

The role of convergence

It was discussed whether convergence should still play a role in the agenda setting. It was noted that EFRAG's draft comment letter presented the view that convergence cannot be the driver of agenda setting. The EFRAG PRC / Supervisory Board member noted that convergence should be understood as bringing different sets of accounting standards closer together and that process is not limited to US GAAP. In fact, convergence with Chinese or Japanese GAAP should be also considered as long as it results in the improvement of the resulting global standard.

A participant from an employer's organisation did not agree with EFRAG's initial thoughts. He thought the IASB should benefit from the amount of experience accumulated in the US over the time. US and China are large countries, which need to have a voice within the IASB. A banking representative underlined that the two biggest economies going their own way in accounting is not a good solution: convergence is relevant but should not be the overall objective.

The EFRAG PRC / Supervisory Board agreed that the IASB should not disregard other jurisdictions as it would not be beneficial for the world economy.

The DASB Chairman thought the wish for convergence was also a political issue and is also a means to get the US adoption of IFRS standards. He commented that all standard setters should work with the IASB, but rather for the purpose of getting high-quality standards, not merely for the purpose of convergence. However, he noted that on financial instruments, despite the various G20 calls for a single set of global standards, the FASB and IASB seem to go for different solutions leading to deferral of the project rather than to decisions.

Participants from audit firms found that starting new phases of convergence through additional memorandums of understanding with other jurisdictions would be troublesome. In addition, the different backgrounds of jurisdictions could justify different principles. This was the case with the Insurance Contracts project, for which the IASB and FASB in certain areas had reached different tentative decisions. They felt in that respect that convergence would never be achieved unless a consistent Conceptual Framework would be in place.

A participant from EFRAG TEG noted that the insurance contract case could be extended to other projects. He thought that it would be beneficial if the Boards could find an appropriate level of agreement or disagreement ('agree to disagree'). If the Boards, for example, agreed on 90% of the issues, they should assess, considering the expected time and resources needed, whether further discussions could result in more converged standards and probably conclude to continue issuing the standard.

From a preparer's perspective, a participant believed that in the last five years, the joint efforts for achieving convergence have been unsuccessful. However, he expected that convergence would still be an objective for the next four or five years, therefore it would be fair to say that convergence should not be the primary objective but rather a secondary, relevant objective for the standard setting process.

Enhancement of the Conceptual Framework

In its draft comment letter, EFRAG agrees with the IASB's request that one of the projects and priorities of the IASB should be the enhancement of the Conceptual Framework. EFRAG also states that unless there is strong and convincing arguments for the contrary, new standards that are in conflict with the Conceptual Framework should not be issued until a more fundamental debate has been had on the issue in question.

At the event, the EFRAG PRC / Supervisory Board member noted that the proposals for enhancing the Conceptual Framework also include the development of a Disclosure Framework.

The IASB member explained that the IASB had only completed the first steps towards a new Conceptual Framework. The overall objective is to create a sound foundation for future accounting standards. It is a joint convergence project conducted in different phases and only one phase had been finalised. He believed that definitions of elements and measurement are the most difficult parts, which are still not finished. Although a lot of work had been done in the last three years regarding the definition of assets and liabilities, the academic research is still going on.

The IASB member also highlighted that the Conceptual Framework and the projects that had been either postponed or put to a hold were highly interlinked. Sometimes the Board did not have a basis in the Conceptual Framework, as currently drafted, to base itself on when developing a standard. In those situations they have two alternatives: (i) they could either complete the project and the Conceptual Framework simultaneously, or (ii) they could focus on finalising the Conceptual Framework before developing the standard. Different views are held by IASB members.

The DASB Chairman believed that the Conceptual Framework should be completed as soon as possible without striving for perfection. The IASB had been working on this project for a long time and its incompleteness is unhelpful for the discussions and due process.

The EFRAG PRC / Supervisory Board member believed that the conceptual debate and the development of new standards could take place at the same time. He would support amending

the Conceptual Framework if it was generally agreed that the principles would not result in the preferred outcome when developing a particular standard.

The majority of the participants, including users, preparers and auditors agreed that completing the Conceptual Framework should be a priority and should also include the development of a Disclosure Framework. Participants highlighted that disclosure requirements are spread in different standards, which make them sometimes inconsistent.

Request for a period of calm

The IASB member noted that a stable set of IFRS standards had been in place since 2005. Only one standard with significant impacts, IFRS 3 *Business Combinations*, was added to this platform. He believed the next platform would be established around 2015, when the four main projects currently on the IASB work plan would be implemented (i.e. the standards on Revenue from Contracts with Customers, Leases, Financial Instruments and Insurance Contracts). In addition to identifying the projects that should be included on the agenda, deleted or postponed, the IASB would also appreciate participants' views regarding the need for a stable platform of standards.

Participants generally agreed that a period of calm would be appreciated once the four main projects would be finalised. The EFRAG PRC / Supervisory Board member highlighted that a period of calm was a precondition for achieving what EFRAG argued should be the most important objectives of the IASB: (i) to mitigate the risk that evolutions and changes to IFRS standards would not be well understood by users and preparers, and (ii) to mitigate the risk that IFRS standards would not be implemented in a consistent manner by those already applying them or moving to their adoption.

Specific projects to be included on the IASB's agenda

The role of EFRAG proactive projects

Participants agreed that EFRAG's proactive projects on Business Combinations under Common Control (BCUCC) and on a disclosure framework should be amongst the first priorities of the IASB.

A banking participant wondered whether BCUCC was an issue big enough to start such a broad project. After reading EFRAG's proactive paper, the participant felt it was a very complex project to add to the agenda.

The other participants believed unanimously that BCUCC was an important issue to deal with due to diversity in practice within and across jurisdictions. The DASB Chairman noted that quite some people found BCUCC troublesome, and a project on the issue has been requested from early 2004. The EFRAG PRC / Supervisory Board member noted that EFRAG had selected the topic because its Planning and Resource Committee (PRC) thought it was an important issue for constituents. One participant from an audit firm noted that it was already identified as a

significant and widespread issue in the EC Roundtable for the consistent application of IFRS and that the European Commission had written directly to the IASB asking for guidance.

A participant from EFRAG TEG stressed that group restructurings are more and more common in the Netherlands. Difficulties are, for example, encountered in practice with accounting for intra group transfers when there are minority interests. He thought that the amount of literature dealing with the topic (e.g. the manuals prepared by audit firms) was a clear indication that an issue exists.

Regarding the Disclosure Framework, the DASB Chairman mentioned that the New Zealand Institute of Chartered Accountants in partnership with the Institute of Chartered Accountants of Scotland had prepared a paper on disclosures. This paper was presented to the IASB in July 2011 and focused on reducing disclosures.

A user noted that he would focus on providing relevant information to users rather than on reducing the number of disclosures. Many figures that are currently included in the notes are very difficult to interpret. He believed disclosures would be more helpful if they depicted information critical to valuing companies. The participant claimed that financial statements of a parent company, from his point of view, provided little value to investors and could thus be suspended. Another user highlighted the importance of segmental disclosures for company analyses and agreed with the general idea of reducing disclosures. This idea was also shared by two participants from audit firms. One of them suggested that the IASB should adopt a holistic view when reviewing disclosures. Another participant from an audit firm suggested that the reduced disclosure requirements in IFRS for SMEs could be a good starting point for full IFRS.

The IASB member and other participants noted that the European Securities and Market Authority (ESMA) was working on a project on the concept of materiality and will publish a paper for public consultation. The objective was to analyse and identify the principles of a common approach to be considered by European accounting enforcers. Although the IASB was not part of the working group, the IASB member noted that the results could be interesting. The member reminded that IAS 1 *Presentation of financial statements* already included a general concept of materiality and believed it would be beneficial to have a common understanding of the term among affected groups. ESMA's initiative was welcomed by participants; particularly because it was believed that there were different views on how to consider materiality with respect to disclosures. A participant with enforcement background saw a need for coordination between ESMA and National Standard Setters.

The EFRAG PRC / Supervisory Board member noted that materiality on disclosures was a topic that interested preparers, auditors, users and supervisory bodies. The above mentioned project would have to deal with those situations where the supervisory bodies required mandatory information. One participant suggested that the IASB should develop guidance on how to consider materiality with respect to disclosures and not leave this to other parties involved. Another participant believed that it would be better to define principles rather than rules on

materiality. The application on these principles should then be up to the company and the auditor.

The IASB member observed that users are always asking for more disclosures instead of less. This demand has increased the number of disclosure requirements in the standards. In addition, deciding on disclosure requirements is not straightforward as disclosures that would be important for one entity would be less relevant for another.

Regarding EFRAG's proactive project on income tax, a participant from an audit firm was not sure whether IAS 12 *Income Taxes* was sufficiently broken to suggest the IASB to deal with the project. The participant acknowledged that IAS 12 is very granular and has a significant impact on the financial position of companies, thus he suggested concluding based on evidence.

A participant from EFRAG TEG expected that EFRAG would issue its proactive paper on income tax in December. He observed that constituents were split on the issue. Some thought that the current IAS 12 is appropriate while others thought a fundamental review would be necessary. Accordingly, the first part of the paper would propose some short-term improvements, including the discounting of tax provisions. The second part would be more focused on the strategic direction to be followed, if it were to be concluded that a fundamental comprehensive review would be needed.

Projects suggested by participants

The unanimous position of participants was that the IASB should complete the projects it has on its agenda regarding revenue recognition, leases, financial instruments and insurance contracts before undertaking any new project. Some participants thought that it particularly is important to finalise the projects on financial instruments and insurance contracts. Participants recommended the IASB to finish the different phases on financial instruments as soon as possible. A participant from an employers' organisation thought it is important to finalise the four main projects within one year.

The IASB member noted that the IASB's Request is based on the presumption that the IASB is going to finish the four main projects. He noted that the Insurance Contracts project could take longer time to finalise than the other main projects.

The IASB member suggested to focus the discussion on other specific projects participants thought should be included on the IASB's agenda and on what projects should not be included. The IASB is also looking for new project suggestions not included in the annex to the IASB's Request.

Participants thought the following projects should be considered by the IASB:

- Conceptual and Disclosure Framework;
- Other Comprehensive Income;

- Presentation standard;
- Business Combinations Under Common Control; and
- Employee benefits.

(The list is based on participants' opinions as expressed at the outreach event. The order does not reflect any ranking.)

The participants from audit firms insisted that a project that could provide a clear and appropriate distinction between items recognised in profit or loss and in other comprehensive income is necessary. The project should also focus on the recycling mechanics between the two statements.

A preparer thought that projects such as other comprehensive income and revenue recognition were dealing with conceptual issues and should therefore be dealt with at a conceptual rather than standard level. However, the participant believed the above indicated projects were the more important and urgent ones, and it was only a matter of approach.

Regarding the financial statement presentation standard, participants had different views on the merits of the previous IASB staff draft and believed it was also highly related to the discussions on the Conceptual Framework and Other Comprehensive Income. There is a high demand for performance measures. A participant highlighted that currently companies were providing different performance measures and aggregating different profit or loss lines to come up with certain subtotals. More consistency could be achieved through a presentation standard. It was observed that any project on performance measures requires a substantial involvement of users.

The DASB Chairman thought a comprehensive review of employee benefits accounting was needed. Despite the fact that the IASB had recently amended IAS 19, it is a too deterministic, rule-based standard. In particular, a review of the standard would be necessary in order to define appropriate accounting for more recent or 'modern' schemes, which combined features of defined plans and defined contribution plans, and for risk sharing features. From a user perspective, one participant believed it was inconvenient to reopen the debate again just after the latest amendments have been issued. He agreed though, that uncertainty regarding the treatment of risk sharing features still exists. A user agreed and believed that more transparent information was needed for defined contribution plans.

Participants also made some comments regarding the following topics:

- Country-by-country reporting;
- Discount rate;
- Emissions trading schemes;
- Equity method;

- Extractive activities;
- Intangible assets;
- Islamic transactions;
- Liabilities; and
- Management commentary

The DASB Chairman questioned whether country-by-country reporting was a general financial reporting need or a specific request of the European Commission. One user noted that geographic exposure information was useful but, from his point of view, it could be provided outside the financial statements.

The discount rate was a topic of interest because it was a cross-cutting issue and had been debated during the Insurance Contracts project discussions. Participants believed the problem arose as a result of the different objectives of discounting set out in various standards.

A project on emissions trading schemes was considered important for energy companies. Participants agreed that currently entities account for the schemes differently which reduces comparability. However, participants did not consider it as an urgent project.

Regarding the project on the equity method, a participant from an audit firm noted that constituents were unsure whether the method should be considered as a valuation or a consolidation method. A user commented that IFRS 11 *Joint Arrangements* required equity accounting for certain arrangements. He believed it would be helpful to review the equity method. A user noted that the requirements for intangible assets resulted in many difficulties for analysts. There are significant differences in how performance is reported depending on whether the intangible asset had been acquired or internally generated. A participant from EFRAG TEG believed that many projects were linked somehow to the Conceptual Framework and could not be changed without dealing with the Framework first. In that sense he agreed with the user's comments and referred to EFRAG's proactive project on the role of the business model in financial reporting. He noted that the current requirements resulted in the best performing pharmaceutical companies' reporting high losses.

The DASB Chairman asked whether it was necessary to have specific requirements for Islamic transactions. The IASB member thought the objective of the project should be to provide some guidance that would result in Islamic transactions being accounted for in a manner that would be comparable to non-Islamic transactions. He noted, however, that the IASB had not yet considered the topic.

Participants would not support a project on liabilities if the objective of such a project was to require liabilities measured at a probability weighted expected value.

A user asked whether management commentary should be an integral part of financial reporting. The IASB member replied that management commentary was not part of the financial statements, although there is a linkage. He noted that the IASB had no particular authority to require the use of a management commentary and that the authority rests within individual jurisdictions that can require a management commentary. Other participants believed that a new IASB standard on management commentary would not be helpful. A participant from EFRAG TEG mentioned that part of the debate relating to EFRAG's proactive project on a disclosure framework focused on differentiating between information that should be included in the notes to the financial statements and information that should not. Information about key management remuneration could be relevant for users, but it is not relevant in explaining the financial position of a company. It could therefore be questioned whether that information should be included in the notes to the financial statements.

Participants thought the least important project to be included on the IASB's agenda were:

- Agriculture;
- Earnings per share;
- Financial instruments with characteristics of equity;
- Foreign currency translation;
- Government grants;
- Inflation accounting;
- Interim reporting;
- Rate-regulated activities; and
- Share-based payments.

The DASB Chairman anticipated that the IASB would receive many contradicting comments on what project it should include on its agenda. He asked how the IASB should and would decide on this. A participant with a preparer background thought that priority should be given to general projects and that would thus affect many entities.

The IASB member believed that the selection of projects to be included on the IASB's agenda should be based on the convincing evidence and arguments presented to the Board for including a particular project. The IASB would accordingly not base its decisions on the number of comment letters supporting a particular project, but on the arguments presented in favour of including a project. The IASB member noted, however, that it was the first time the IASB addressed agenda setting through a public consultation and it would therefore also have to learn how to deal with the various priorities expressed by constituents.

Other issues

A participant from an audit firm noted that EFRAG's draft comment letter does not include any reference to the role of the IFRS Interpretations Committee (IFRSIC), although the IASB Agenda Consultation paper includes some references. From his point of view, the IFRSIC should be more involved in the agenda setting process and improve its own effectiveness. Furthermore, the IFRSIC should be careful that its decisions do not become application guidance of IFRS standards. A user asked to consider the introduction of a fast track procedure to urgently deal with upcoming (interpretation) issues.

The IASB member noted that the IFRS Trustees were reviewing the effectiveness of the IFRSIC and mentioned the appointment of Wayne Upton as its new chairman as of July 2011.