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Dear Sir/Madam

RESPONSE OF THE ACCOUNTING COMMITTEE OF CHARTERED ACCOUNTANTS IRELAND

EFRAG/ASB DISCUSSION PAPER: CONSIDERING THE EFFECTS OF ACCOUNTING STANDARDS

The Accounting Committee ('AC') of Chartered Accountants Ireland welcomes the opportunity to comment on the proposals of the European Financial Reporting Advisory Group ('EFRAG') and the UK Accounting Standards Board ('ASB') in the abovementioned discussion paper.

Our comments on the specific questions asked in the document are contained in the attached appendix.

Yours faithfully

Mark Kenny
Secretary to the Accounting Committee

APPENDIX

SECTION 2: THE PROCESS OF 'EFFECTS ANALYSIS'

Q1: 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)?

If you disagree with the proposed definition, or would like it to be amended, please provide an alternative definition, and please explain why you favour that alternative definition.

AC agrees with the definition and agrees that the alternative 'impact assessment' definition would suggest a deeper cost/benefit analysis and does not get the message across that it should be a process to be integrated into the overall standard setting procedure. AC notes that a more qualitative approach rather than a quantitative process is being proposed.

Q2: 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? Please explain the reasons for your answer.

AC agrees that effects analysis should be integrated into the standard setting process as that can only strengthen that process and provide clear transparency to users and preparers that all potential effects are considered before issuing a standard. That can only help the credibility and accountability of the standard setters and maintain confidence in the process.

Q3: 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)? If not, why not? Please explain the reasons for your answer.

Whilst it might be considered preferable for an independent body, such as a securities regulator or other government agency, to be involved in the effects analysis, AC notes a number of practical difficulties in this regard. Firstly, the IASB produces international standards, and there is no obvious global body which could carry out the effects analysis. Whilst there are existing bodies that could take that role on in individual countries or groups of countries (e.g. ESMA and the SEC), they may not come up with the same conclusion, which would lead to diversity in accounting practice. Secondly, the collection of information on effects and the development of proposals for new standards are very much intertwined, such that it would be very difficult to separate the two functions effectively.

Therefore, AC considers that the IASB should be the body performing the analysis. AC notes that there could be a perception that the standard-setter has an in-built bias towards publishing a full standard and believes, therefore, that in undertaking this function, it is very important for the standard-setter to be seen to be liaising with those affected by the proposed standards, not to be unduly swayed by commercial and political considerations, and to be clearly acting in a neutral manner on behalf of the public interest.

Q4: 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.**

If you do not agree, why is this? Please explain the reasons for your answer.

AC agrees that the 'effects analysis' should be a process that is carried out at each stage of the standard setting operation i.e. from discussion paper to final standard and disclosed for commentators to assess. However, it would be very difficult to carry out a detailed assessment at the agenda decision point in time given that there are no proposals at that point. As such, any assessment at this stage is likely to be very high-level, though AC still considers it appropriate that the assessment is undertaken. The standard setting process can only deal with anticipated effects which may not occur so a post implementation review should also be undertaken to find out whether the actual effects turn out to be what was expected and, if not, to assess whether there a case for altering the standard accordingly.

Q5: 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 (paragraph 2.19)? If not, why not? Please explain the reasons for your answer.

AC agrees that minor amendments should not involve any detailed, if any, effects analysis. For controversial and highly sensitive topics, it is considered vital that a major effects analysis is undertaken as the proposed standard undoubtedly will have major consequences. Time should not be a major consideration and standards should not be rushed through without proper analysis of their likely impact.

SECTION 3: THE CONCEPT OF 'EFFECTS'

Q6: 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)?

If you disagree with the proposed definition, or would like it to be amended, please provide an alternative definition and please explain why you favour that alternative definition.

AC would not be overly concerned about the definition of effects as opposed to alternative titles such as consequences. The literature over the last 30 years, however, does refer to economic and political consequences (e.g. Zeff in USA, Bromwich in UK). The important point is that both qualitative and quantitative 'effects' must be considered both in terms of their micro impact on individual entities and their macro impact on the economy and society as a whole. The definition above, therefore, seems to be perfectly fine.

Q7: 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)? If not, why not? Please explain the reasons for your answer.

AC would agree with the comment in paragraph 3.7 which would suggest that costs and benefits are a subset of effects. They are the quantitative side of effects but the qualitative side should also be considered. AC would therefore prefer to adopt the term 'effects'.

Q8: 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)?

If you disagree, please provide an alternative way of specifying what the scope of the 'effects' to be considered should be, and please explain why you favour that alternative.

As noted in AC's reply to question 6, AC agrees that both micro and macro impacts be considered in the 'effects analysis'.

Q9: 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)? If not, why not? Please explain the reasons for your answer.

The IASB/standard setter should clarify what its role is in relation to the standard setting process. If there is a perceived expectations gap on what the standard setter can achieve (e.g. current financial crisis), then AC agrees that the standard setter should communicate with the relevant regulator to see what they can do to intervene and ameliorate the consequences associated with that effect. However, as mentioned previously, this would not be a global solution, as each jurisdiction has its own regulator.

Q10: 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)?

If you disagree because you consider that 'effects' should not be defined by reference to an objective, please explain the reasons for your answer.

If you disagree because you consider that 'effects' should be defined by reference to an objective other than that specified above, please provide an alternative objective and please explain why you favour that alternative objective.

AC agrees that any process introduced by a body must have an objective and, clearly, what the standard setter is trying to achieve is to develop a set of accounting standards that find acceptability throughout the constituency for which it serves. The term 'public interest' is appropriate as financial reporting has broadened out to serve the interest of a wide range of users including government, the public, employees, creditors as well as existing and potential investors. AC considers that primacy should be given to the impact of accounting standards on users rather than preparers of financial statements.

Q11: 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 'on-going 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)?**

If you do not agree with any of the above clarifications of the term 'effects', which one(s) do you disagree with and why? Please explain the reasons for your answer.

AC accepts that effects can be positive, negative or even neutral in their impact, but would always have assumed that this was the case and therefore does not need to be explicitly stated. It is, certainly, the marginal impact, rather than the absolute impact, that should be considered, because the standard setters must be concerned with the likely impact on the current status quo. It should also include both one-off and on-going effects, although the latter is more important in the long term – there may be short term problems when introducing a standard which should not impinge on a more considered long term view (e.g. the one-off tax impact under UK and Irish GAAP of the publication of Urgent Issues Task Force (UITF) Abstract 40 *Revenue recognition and service contracts,* which applied the provisions of FRS 5 *Reporting the Substance of Transactions* Application Note G *Revenue Recognition* on long-term contract accounting to all contracts for services).

As previously noted in our comments to Question 4, both anticipated and actual effects must be investigated by the standard setter for major projects.

Q12: 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);**
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)?**

If you do not agree with any of the above further considerations concerning effects, which one(s) do you disagree with and why? Please explain the reasons for your answer.

AC considers that, as noted in the reply to question 10, the effects on users should have primacy.

In relation to the Board's further preliminary views as set out in paragraphs 3.30 to 3.32, AC considers them appropriate in principle. However, given the limited level of experience and precedent in this area of standard setting, AC considers that the practical operation of this approach to effects analysis should be assessed by the Board after an initial period of operation.

SECTION 4: THE KEY PRINCIPLES UNDERPINNING EFFECTS ANALYSIS

Q13: Do you agree that there should be a set of key principles underpinning effects analysis (paragraph 4.2)? If not, why not? Please explain the reasons for your answer.

AC agrees that, as long as there are broad principles, which is the case with the four listed in paragraph 4.2, there is a benefit in including these as guidance to the standard setter when undertaking an 'effects analysis'.

Q14: 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)?**

If you disagree with the proposed set of key principles, or would like the principles to be amended, please provide an alternative set of key principles and please explain why you favour that alternative set.

As noted above, the four principles are fairly broad and cover the process very succinctly. AC would therefore support the proposed set.

SECTION 5: THE PRACTICALITIES OF PERFORMING EFFECTS ANALYSIS

Q15: 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?

If you disagree with the proposed steps, or would like the steps to be amended, please provide alternative steps and please explain why you favour those alternative steps.

AC would support the initial process suggested in paragraph 5.2 that, before a project is undertaken, it should be reviewed for current treatment (i.e. literature review), confirm that there is a problem and ensure that any benefits are likely to outweigh costs and the extent of diversity in practice, et.al. This view supports the comments made by AC in relation to question 4.

Q16: 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?

If you disagree with the proposed steps, or would like the steps to be amended, please provide alternative steps and please explain why you favour those alternative steps.

AC would support broadly the steps in paragraph 5.3, but considers that, perhaps, the description of the steps contains too much detail, e.g. use of relevant models, marginal and absolute effects, one-off and on-going effects etc. The steps could be simplified in a manner similar to the principles in paragraph 4.2.

Q17: 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?

If you disagree with the proposed steps, or would like the steps to be amended, please provide alternative steps and please explain why you favour those alternative steps.

AC would again argue that there is too much detail in guiding standard setters to choose the preferred option. As per question 16, it would rather support a series of simple steps without getting involved in detailed ‘effect adjustors’ etc.

Q18: 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)?

Clearly the IASB, as the global standard setter, must liaise with national standard setters who could carry out a lot of the analysis. However, different national bodies will undoubtedly provide conflicting results (e.g. the differing attitudes of some jurisdictions to the IFRS for SMEs). It is important that the IASB gathers all available evidence from those institutions and, using its own judgment, gives a global view of the ‘effects analysis’.

SECTION 6: NEXT STEPS

Q19: 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?

If you disagree with the proposed next steps, or would like there to be additional next steps, please provide alternative and/ or additional steps and please explain why you consider that those alternative and/ or additional next steps are appropriate.

AC agrees that the next step should be to field test the development of a live IFRS, however AC believes that the proposals should only refer to the future work plan of the IASB and should not delay any of the major projects on the IASB’s current work plan.

In this regard, AC considers it important to recognise, and give credit for, the extensive outreach efforts currently being undertaken by the IASB in developing new standards, for example the various roundtables taking place across the globe on different issues.

AC would agree with national standard setters sharing their knowledge to date of such issues, for example if some have already implemented elements of the proposals in their jurisdictions, or if they have undertaken consultation processes and/or field testing with their constituents.