DUTCH ACCOUNTING STANDARDS BOARD (DASB)

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Date : Amsterdam, 31 August 2011
Re : Comment on the Discussion Paper "*Considering the Effects of Accounting Standards*"

Dear members of EFRAG,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to respond to the Discussion Paper "Considering the Effects of Accounting Standards".

In general, we consider this is an admirable paper, for which there is a significant need in practice. As a consequence, we are highly supportive of issuing this discussion paper in its final format.

However, we do have certain concerns with some aspects of the paper.

Our main concern is the question of how these proposals can be rapidly converted into a actual and practical process. In this connection, we believe that there should be more focus on outcome rather than the process alone, i.e. that it should be clear from the outset (agenda-proposal) what the purpose of "effects analysis" is in each step of the standard setting process and what conclusions can potentially be drawn from it. There is a significant inherent risk of bureaucratisation and of a "one size fits all" process. Proportionality should be a key element upfront to avoid a overtly complex, if not excessive, process.

As we have set out in our response to question 13 regarding the four principles outlined in 4.2 of the document, we believe the language used there should be clarified and that the visibility as to how these key principles are to be used in practice should be enhanced. We also believe that the process is an iterative one and this should be made clear as well.

In our opinion, from a governance point of view this process should be under independent oversight to ensure balance in any conclusions drawn from it and in particular with regard to decisions on any action (or no action) taken in the further development (or amendment) of a standard. This is also necessary to ensure that the process is balanced, eliminates subjectivity as much as possible, and perhaps more importantly that its outcome is fit for purpose and does not result in “predictable” or “preferred” conclusions.

That independent oversight is the more necessary because it will be difficult to weigh qualitative aspects in terms of “costs” and “benefits”; these often will need to be viewed in a broader context and it may not always be easy to substantiate the outcome with evidence. Also, a completely objective decision will in many cases be impossible because the same effect may be perceived as positive for one and negative for another.

As a consequence, it will be important to ensure transparency in how conclusions were reached, i.e. which arguments were used and how effects and arguments were weighted in reaching conclusions and decisions on any resultant action (or not).

We believe that the oversight aspect outlined above should be stressed more in the paper as written.

We refer to the appendix for our detailed responses to the questions you have set out in the discussion paper.

Yours sincerely,

Hans de Munnik
Chairman Dutch Accounting Standards Board

APPENDIX 1 – Responses of DASB to the questions

SECTION 2: The process of 'effects analysis'

Question 1
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.

In our opinion, the definition should have more focus on the outcome rather than the process, so that it is clear from the outset what the purpose of the "effects analysis" is and what conclusions can potentially be drawn from it. In our view the definition should be expanded and read:

"a systematic process for considering the effects of accounting standards and including the conclusions of such considerations as those standards are developed and implemented"

We also refer to our response to question 6 on "intended" consequences. Should that reference be considered for inclusion in the definition? In other words, should the above definition be further expanded by adding for instance:

"...to ensure that those standards do not result in unintended consequences" or:

"...to ensure that the final standards will continue to meet the intended effects as defined in the related objectives for those standards".

Question 2
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.

Yes we agree. This should be an iterative process where conclusions should be fed back into the development cycle, in order to avoid that this process will add another bureaucratic layer.

Question 3
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.

Yes, we agree that performing effects analysis should be the responsibility of the standard setter. That would fit with the premise that it is an integral part of the standard setting process. However, we also believe that this process should have independent oversight to ensure balance in any conclusions drawn from it and in particular with regard to decisions on any action (or no action) taken in the further development (or amendment) of a standard. This would be especially relevant where any potential "go/no go" issues are encountered. We are currently unsure whether such an oversight function can be accomplished within the existing IASB governance structure, but this should be food for consideration in the review by the Foundation and the Monitoring Board.

Question 4
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 “postimplementation 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.

Yes we generally agree, but also believe that each of those steps should be proportional to the potential effect, an aspect raise in the next question. It should not be a “one size fits all” process to avoid this becoming overly complex if not excessive. For instance, a relatively minor amendment, that is generally supported, should require a less onerous analysis than a completely new standard or a fundamental review of an existing standard.

In that context, point A should also make clear what “effects analysis” in each of the life-cycle steps of developing a standard (or amendment) is expected to be required or contemplated to ensure absolute clarity from the very start about the goals and purposes of any project. We also refer to our response to question 1, where we stated that there should be more focus on outcome rather than only the process itself. In addition, mainly with reference to point E, we believe that one should be careful that standards do not keep on changing. Any change should be motivated and be based on real issues experienced in practice or significant unwarranted effects rather than theoretical niceties.

We do believe that assessing the effects in an early phase will contribute positively to the standard setting process, but the bigger question in our view is how these effect studies will be carried out.

Question 5
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.

Yes we agree. We also refer to our response to the previous question.

How this will work in practice is something that needs further work in our view. For example, what about a potentially very high impact amendment that will only affect a small group of preparers? How will that be balanced with the (perceived) need of users?

We also wonder what exactly is meant by "available time" in this context. In our view, available time should not be the only or overriding argument in any decision on the scope of an effects analysis. The decision to undertake an effect study and the way this is carried out should consider all relevant factors as part of a careful evaluation process.

SECTION 3: The concept of 'effects'

Question 6
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.

We do not entirely agree.

In our view, standards (or amendments thereto) as a whole should be referenced against the objectives of serving the public interest; consequences (or effects) will then automatically flow from there because they are the "intended" results of the process. The ultimate issue really is the avoidance of "unintended" consequences; effects analysis should ensure that any step of the development cycle of a standard (or amendment thereto) continues to result in "intended" consequences. We believe that this latter aspect could be usefully considered in the definition of an effects analysis, as we have suggested in our response to question 1.

The definition should also be more clear about which consequences are exactly meant. In section 3.23-3.25 of your discussion paper the effects are clearly set out. That clarity (consequences are effectively equal to effects) should also be incorporated more explicitly in the definition, so that it will be unequivocal that not only positive consequences but also negative consequences –like more costs- are included. Also, improved financial reporting should not always be equated with more information, an aspect of which the definition is somewhat suggestive. The possibility that information remains the same, but is for instance relocated in the financial statements at a lower cost to preparers, does not appear to be covered in the definition.

We also believe that the last part of the definition '*contributing positively to delivering improved financial reporting*' needs some fine-tuning. We wonder why this text is not aligned with the stated objective of the IASB as included under 2a in the IASC Foundation Constitution. We would in any case suggest the deletion of the word 'positively' because this is already covered in ‘contributing’ and believe that the word ‘improved’ should be replaced by ‘high quality’.

On a final note we would replace the word “flow” in the definition with the word “result”.

Regarding ‘public interest’, we also refer to our response to question 10.

Question 7
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.

In our opinion, the CBA should not entirely be left out. We agree that CBA should not be the primary tool, but a review of quantitative aspects will be particularly useful in evaluating the costs. Benefits on the other hand can be difficult to measure as they cannot always be expressed in amounts and should therefore be seen in a broader perspective. This should also be evaluated on a case-by case basis, with reference to the section 2E of the discussion paper, ‘Proportionality in performing effects analysis’. Some new or amended standards could have more quantitative effects, while other could have more qualitative effects. It should be clear that the conclusions should not only depend on a 'math' / quantitative evaluation.

We believe that it can be difficult to substantiate the outcome with evidence and that this will need more consideration. We believe that it is impossible to gain a complete objective decision, as the same effect can be positive for one and negative for another. We stress the importance of transparency of how conclusions were reached, which arguments were used and how effects and arguments were weighted to come to the conclusions and the decisions on any resulting actions (or not).

In a relatively recent impact study here in the Netherlands on a change in the Dutch GAAP pension standard we reached the following conclusions. Outcome was that costs would decrease (especially due to the reduced need for the use of an actuary for calculations in addition to already available information), and that the standard was more aligned with other pension reporting obligations. The latter had a positive effect, but could not be expressed in terms of amounts.

Question 8
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.

Yes, in principle we agree, but we believe that macro-economic effects will be hard to identify in practice. It is highly questionable whether it is possible at all to assess macroeconomic effects in advance, in addition to defining and determining what a macro-economic effect is or could be. For instance, if a new standard delivers better information and users take different decisions on the basis of this improved information, is that a macro-economic effect? And should that then be qualified in terms of good or bad?

Macro-economic effects should not be scoped as such out but should be limited to a description of any potentially discernible effect in the respective step of the development cycle of a standard.

Question 9
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.

No, we do not agree. We believe a communication requirement of any such effect is in order, but in our opinion it is beyond the remit of a standard setter to explicitly obtain a confirmation from a regulator or government body that they will make an appropriate response. In addition, it is unclear to us what the consequence would be for a standard setter if such a response is not forthcoming, inappropriate or much delayed.

Question 10
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.

We refer to our response to question 6.

In addition, we believe that 'preparers' should also be included in the meaning of "serving the public interest".

Question 11
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 “ongoing 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.

Yes, we agree.

Question 12
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); and

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 or your answer.

A) We agree, but also refer to our response to question 3, where we stressed the need for independent oversight of this process to ensure that the process is balanced, eliminates subjectivity as much as possible, and perhaps more importantly that its outcome is fit for purpose and does not result in “predictable” or “preferred” conclusions.

B) We agree with some sort of “ranking” system, but this may need to be tailored to the specific circumstances. Additionally, magnitude is not well defined, i.e. how do you measure that in terms of qualitative aspects? And how would one weigh qualitative aspects that are in any case difficult to measure. For example, a change that results in less disclosure requirements is probably somewhat measurable, but an increase in disclosure requirements will probably be harder to argue in assessing the effects.

   We do not think the table in 3.32 in your discussion paper is particularly helpful in this context; measuring potential risk in our view is different from measuring effects. We would on the basis of the table have trouble in understanding how a standard that affects nearly all (incidence) with negligible consequences (nature) could result in an effect that is determined as significant.

The European Union requires already impact studies for a range of measures and we wonder whether a study thereof would be helpful in this respect. We support the requirement that effect analysis should be performed, but believe that making this a feasible process in practice will need more consideration. A real-life trial run would be extremely good to assess where the strengths and weaknesses are in such a process.

SECTION 4: The key principles underpinning effects analysis

Question 13
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.

We have the following comments to the key principles:

- None of the key principles requires conclusions, decisions and actions; they only require in key principle 4 consideration of effects without spelling out that something should be done with the assessed impact. We have already stressed that this is an iterative process. For example, it is imaginable that at some stage in the development cycle of a standard effects are assessed of such magnitude that it would require a return to the agenda setting stage to re-deliberate the original objective. We see none of this in key principles and believe this should cleared up.
- In a number of instances, i.e. in key principle 2 and the comment text in 4.7, the word "encourage" is used; we have trouble in understanding how "encourage" equates with "key principle"; we have a similar concern with the use of the word "expectation" in 4.6. A key principle should be a requirement and in our view terminology of that nature should be used in all 4 key principles.

Question 14
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.

Reference is made to our response to question 13.

SECTION 5: The practicalities of performing effects analysis

Question 15
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.

Reference to our answers to prior questions.

Question 16
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.

Reference to our answers to prior questions.

Question 17
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.

Reference to our answers to prior questions.

Question 18
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)?

Yes we agree.

<u>SECTION 6: Next steps</u>

Question 19
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.

We agree with the proposal to share the knowledge between national standard setters and similar institutions, as also organized on May 16, 2011 by you.

But we are wondering which project will be proposed and we believe that it will help to mention a specific example of a project in this matter. We suggest this should not be a too complex project and one where a conclusion could be reached within one year. Also, we suggest that this process should be post-evaluated after a certain period. A concrete project proposal would help.

In our view such changes to the standard setting process should also be embedded in the governance of the Foundation. Furthermore, an independent oversight role, which we believe is necessary, should also be included in these considerations. In this respect, there may be a role for the Monitoring Board, too.