



IAASA

Financial Reporting

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- The views expressed are mine and do not necessarily reflect the views of the Board, individual Board members or the staff of IAASA

Section 31

No person shall disclose, except in accordance with law, information that –

- a) is obtained in performing the functions or exercising the powers of the Supervisory Authority, and*
- b) has not otherwise come to the notice of members of the public...*

Certain exemptions provided for in law

Presentation overview

- Financial reporting – the financial crisis in context
- IAASA's role in financial reporting
- Accounting enforcement in an EU context
- Key messages

Principal Functions of Financial Reporting Supervision Unit of IAASA

- To examine whether the financial reports of issuers whose Home Member State is Ireland under the Transparency Regulations complies with the relevant reporting framework
 - Liaising with other countries' financial reporting monitoring bodies
- Co-operating in the development of accounting standards and practice notes
- Assisting the Board to discharge its functions as an advisor to the Minister on accounting related matters

Financial reporting – Putting the financial crisis in context



What's the financial crisis got to do with financial reporting?

**“Did you know
IAS 39 may have
caused the entire
crisis?”**

**“If you change
the accounting
rules you can
make the losses
go away”**

**“Calling it what it
is – Fraud and an
outrage”**

**“Window
dressing... Circular
transactions...
Distort amounts in
the financial
statements”**

**“Financial
statements are a
fantasy”**



Financial reporting implications of the credit crisis

- Going concern
- Impairments
- Asset valuations
- Pensions
- Financial instruments measurement
- Risk disclosures and disclosures in general
- Related party transactions
- Bank covenants



General Purpose Financial Statements

“to provide useful information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions”

(IASB Framework)



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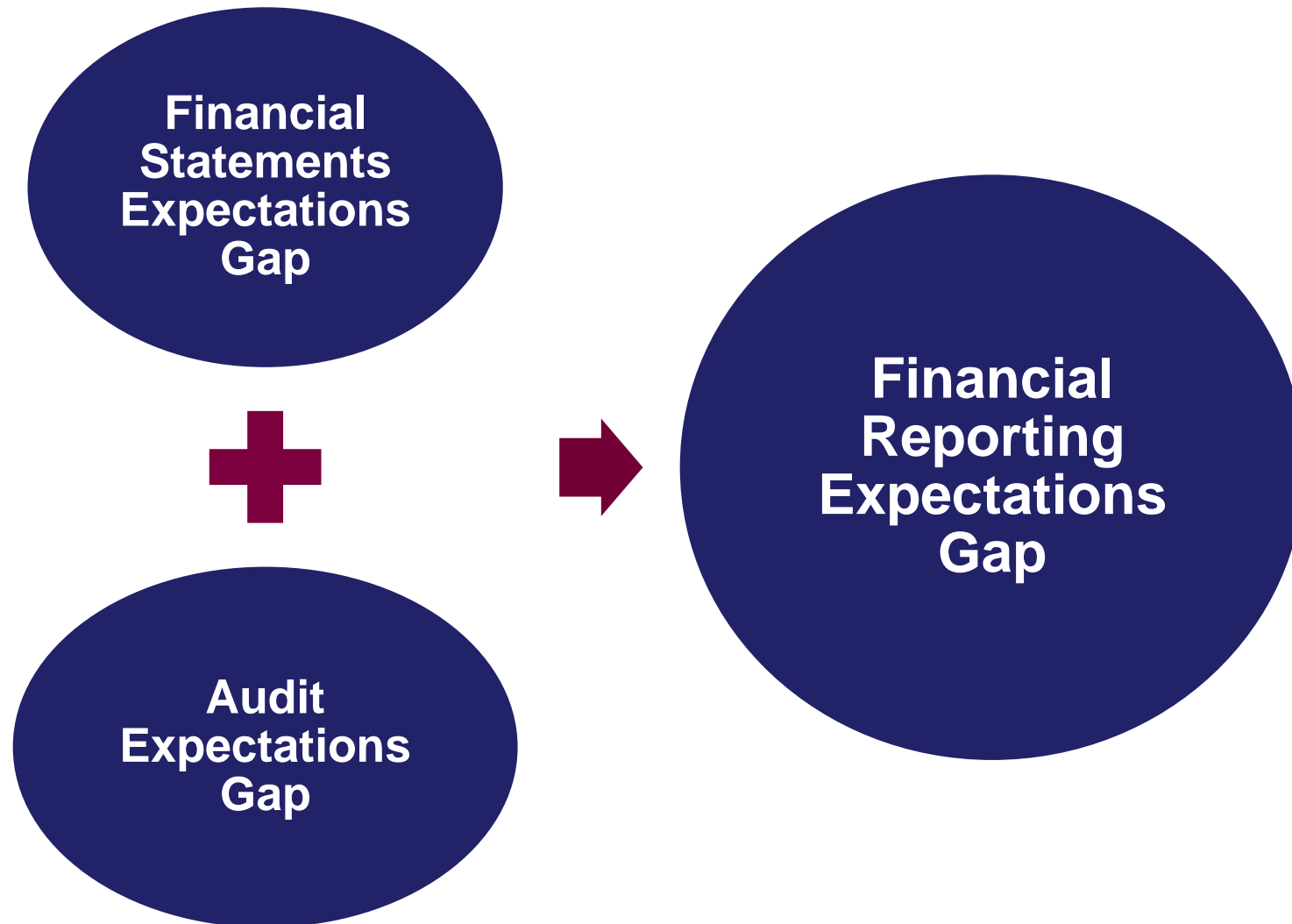
Users of Financial Statements

- Present and Potential Investors
- Lenders
- Suppliers
- Employees
- Customers
- Government and their agencies
- Public

- Decisions about Buy/Hold/Sell
- Stability and profitability of business
- Whether debts will be paid when due
- Regulation of an entity's activities
- Taxation policies
- National Statistics
- Trends and recent developments



Financial Reporting Expectations Gap



Financial Statements – Expectations Gap

The gradual growth of information in financial reporting which had been driven by a need to satisfy every user in detail had changed the nature of the reports. The whole process had become a compliance exercise rather than a communication exercise.

(PM Kam, Member of SAC of IASB)

There are an awful lot of debates about what can be added in but no one ever has discussions about what can be deleted.

(Ian Wright, FRC)

While financial reporting is intended to be a means of communication between companies and the providers of capital, the process has developed to become more useful to accountants, auditors, lawyers and regulators. The original purpose has become lost.

(Bob Herz, FASB Chairman)



Financial Statements Expectations Gap

Suggested causes by various commentators

- Function of the requirements of the relevant Accounting Framework
- Function of managements' interpretations of the requirements of/choices in the relevant Accounting Framework
- Function of management's approach – 'Compliance' versus 'Communication' objective
- Snapshot in time, short-term focus, past events
- Focus on Quantitative/Financial Information
- Limited view of the notion of 'Performance'
- Financial Statements complexity and overload



- Accounting standards and their impact on:
 - Market volatility
 - Pro-cyclicality in credit extension
- FV accounting in illiquid markets
- Off-balance sheet entities
- New model for loan impairments

The world of “tell it as it is” accounting will naturally lead to more volatility in financial results, but the one thing that we know about the world’s markets is that they are volatile.

D. Tweedie (IASB)



Financial Statements – Macro issues

- The nature of accounting – much more art than science – judgments, close calls
- Balance between principles-based and rules-based regulation (incl. in standard-setting, accounting enforcement)

Bob Garnett (IASB) on the introduction of IFRS 7 (A principles-based standard):
“We got a lot of boilerplate... we did not get any useful information whatsoever”

Effective Financial Reporting

(FCAG, 2009)

1

- High quality accounting standards

2

- Consistent and faithful application

3

- Rigorous independent audit

4

- Proactive enforcement

Where does IAASA fit in?



IAASA's financial reporting supervisory/enforcement function

- IAASA is the independent designated competent authority for carrying out functions under Article 24(4)(h) of the Transparency Directive, i.e.

“..to examine that information referred to in this Directive is drawn up in accordance with the relevant reporting framework and take appropriate measures in case of discovered infringements.”

What issuers come within IAASA's supervisory remit?

- Applies to all issuers with securities (debt and equity) admitted to trading on an EU regulated market i.e.
 - Shares
 - Bonds or other forms of securitised debt
 - Derivative securities
 - Units issued by closed-ended investment funds
- Applied for accounting periods **commencing on or after 20 January, 2007**

Review constituency as at 31 December 2009

Category	Number of issuers in category	Half-yearly financial reports issued per annum	Annual financial reports issued per annum	Total no. of periodic financial reports per annum
Equity	31	31	30 [▲]	61
Funds	45	45	39 [▲]	84
Debt	92	67	92 [▲]	159
Total	168	143	161	304

half-yearly financial reports for a period of 10 years

Methodology for selection of entity for review

Selection criteria include:

- Risk of material misstatement in the financial statements
- Potential impact on users of financial statements in the event of material misstatement
- Supplemented with random selection of financial statements for review

IAASA's approach towards issues

- What a review entails.....
- Review issues addressed, in the first instance, through correspondence with issuers with request to respond
- What an IAASA letter contains
- Additional correspondence where further clarification or further elaboration is required
- Where relevant/applicable, further action determined having regard to significance of issues arising and directors' responses to matters arising
- Evolving approach

Responses to matters arising from reviews completed during 2009/(2008)

Issuer category	Number reviews completed	Undertakings regarding future reporting	Publication of amended financial report
Equity	18 (15)	13 (10)	0 (1)
Fund	13 (17)	10 (11)	3 (9)
Debt	17 (19)	10 (18)	5 (18)
Total	48 (51)	33 (39)	8 (28)

Overview of 2010 activities and results



Advocacy

- Observations on Selected Financial Reporting Issues
- Observations on Materiality in Financial Reporting
- Professional Journal Articles
- Engagements with stakeholders and presentations



Matters noted in IAASA Observations 2008 document still relevant and in particular

- Retirement benefits
- Going concern
- Deferred tax assets



IAASA Publication - Observations on selected financial reporting issues - 2009

- Impairment of goodwill
- Hedging instruments
- Bank covenants
- Related party transactions and balances
- Accounting for government grants and disclosure of government assistance
- Materiality
- Financial instruments – risk disclosures
- ‘Operating profit’
- Key performance indicators {KPIs’}
- Management reports
- Reliance on ‘industry practise’



IAASA publication - Observations on materiality in financial reporting

Key messages

- wide range of users of financial statements (over focus on investor needs?)
- whether an omission or misstatement “**could**influence the economic decisions that users make” – not would
- Attributes of the information
- Purpose of the disclosure
- Intentional errors



Accounting enforcement in an EU context

- Transparency Directive requires every Member State to establish an accounting enforcer

“Each competent authority shall have all the powers necessary for the performance of its functions. It shall at least be empowered to:

... examine that information referred to in this Directive is drawn up in accordance with the relevant reporting framework and take appropriate measures in case of discovered infringements”.

- Approximately 6,500 listed companies have been identified by EU enforcers as IFRS users and are under supervision of competent authorities



IAASA involvement in European accounting enforcement

- European Enforcement Co-ordination Sessions (EECS)
- EECS enforcement decision database
- CESR publication of decisions from the database
- IAASA involvement in EECS



Summary and some key messages

- Dealing with IAASA correspondence.....
- Equity issuers (items specific to those reviewed but some remaining common issues)
 - Related Party Disclosures
 - Disclosures in HY Reports (e.g. More explanations of items needed, acquisition disclosures (IFRS 3(R) etc.)
 - Give concise, comprehensive and transparent disclosures in the annual report
 - tell the full story
 - Operating profit and exceptional items
- Debt and Fund issuers – improvements needed



Summary and some key messages (cont.)

- Front end of the annual report
 - Use of potentially misleading non IFRS figures
 - Proper disclosure of risks and uncertainties and management judgements as required by law
 - Overall quality of front end reporting could be improved
- Have more regard to all users needs in accounting for and disclosing information
- Directors bear ultimate responsibility for the financial report and nobody else!
- Preliminary announcements – time to review their role?
- Role of investors
- IAASA reviews – the next three years.....



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