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EACB Response on Status of Trustees' Strategy Review

24 February 2011

The European Association of Co-operative Banks (EACB) is the voice of Co-operative Banks in Europe. It represents, promotes and defends the common interests of its 28 members and co-operative banks in general. Co-operative banks form decentralised networks which are governed by banking as well as co-operative legislation. The co-operative banks business model is based on three pillars: democracy, transparency and proximity. Through those pillars co-operative banks act as the driving force of sustainable and responsible development by placing the individual at the heart of their activities and organization. In this respect they widely contribute to the national and European economic and social objectives laid down in the Lisbon Agenda. With 63.000 outlets and 4.200 banks, co-operative banks are widely represented throughout the enlarged European Union playing a major role in the financial and economic system. In other words, in Europe one out of two banks is a co-operative. Co-operative banks have a long tradition in serving 160 million customers, mainly consumers, retailers and SMEs. They have also developed a strong foothold in the corporate market providing services to large international groups. Quantitatively co-operative banks in Europe represent about 50 millions members, 750,000 employees with a total average market share of about 20%.

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General Comments

The members of the European Association of Cooperative Banks (EACB) welcome the initiative of the Trustees to seek inputs on how to consolidate the accounting standards setter organisation.

EACB appreciates the decision announced on 25 November 2010 to postpone the deadline to 24 February 2011. Notably, this gives the possibility to comment on this consultation in light of the monitoring Board's proposals for the evolution of the IFRS Foundation governance issued earlier this month. However, we have some concerns regarding the ambitious time line for the strategy review provided as an appendix to the consultation paper. Although it seems that the Trustees are still at an early stage of their deliberations, we do not find realistic the objective to conclude the Strategy Review at their meeting in London in March 2011.

We are pleased to express the following on the review:

- **EACB asks the Trustees to closely coordinate the strategy review with the governance review conducted by the Monitoring Board** in order to allow stakeholders to respond consistently to each consultation and avoid any drafting overlap on some issues. EACB took note that the Trustees are looking for comments on the operational aspects of governance, particularly the standard-setter's process. By contrast, the Monitoring Board is looking to receive comments primarily focusing on institutional aspects of governance, particularly the composition and the respective roles and responsibilities of the Monitoring Board, Trustees and IASB. We understand that the two projects have a different scope but are of the opinion that the two projects will inevitably be interdependent and will affect each other.

- The EACB actively participates in the consultation processes launched by the IASB and we recognise the significant efforts made by the IASB to build a constructive dialogue with European co-operative banks. **We are convinced that the quality of the standard setting process forms a major role in our members understanding of the new standards.**

- In this respect, **EACB does not consider that the approach for IFRSs should be exclusively investor-based.** We believe that financial reporting should provide information about the economic resources of an entity and the claims on those resources to all kinds of capital providers, such as equity investors, lenders and other creditors. Moreover, we would equally support a wider scope of stakeholders, notably considering potential interactions with prudential reporting. Furthermore, an extended scope might prove to better understand and respect existing differences among business models as well.

- **The IFRS Foundation should be committed to the public interest.** Therefore, the place and role of the IFRS Foundation three bodies structure should be clarified in order to differentiate between the need for independent high quality execution of standards and the need for a strong accountability framework.

- **EACB suggests the Foundation holds an additional public consultation on the setting of priorities and scoping of the IASB agenda items**. Moreover, we would support impact assessments at different phases of the standard setting process.

- **EACB asks the Trustees to ensure that the IFRSs are clear and comprehensible** as well as capable of being implemented and audited in a practical manner.

Our detailed comments are set out below.

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Mission

How should the organisation best define the public interest to which it is committed?

1. ***The current Constitution states, "These standards [IFRSs] should require high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions." Should this objective be subject to revision?***

2. ***The financial crisis has raised questions among policymakers and other stakeholders regarding the interaction between financial reporting standards and other public policy concerns, particularly financial stability requirements. To what extent can and should the two perspectives be reconciled?***

The members of the European Association of Co-operative Banks agree that high quality accounting standards providing high-quality financial information would contribute to financial stability, and therefore should remain the primary objective of the IFRSs.

Therefore, we have some concerns with the only investor-based approach followed by the IASB. The financial crisis showed that it is expected that high high-quality global accounting standards provide information about the economic resources of an entity and the claims on those resources to all kinds of capital providers, such as equity investors, lenders and other creditors. Thus, **EACB supports a wider scope of stakeholders, including prudential authorities.**

Actually, considering the growing interaction between IFRS standards and prudential requirements, we are convinced that regulators and particularly prudential regulators have a role to play within the standard-setting process. While we recognise that it might not be possible to remove all differences between financial reporting and regulatory requirements, we believe that the IASB and supervisors should work in close cooperation in order to align as far as possible reporting requirements. Therefore, we particularly support increasing cooperation with the Basel Committee when developing a set of high-quality global accounting standards.

Moreover, while co-operative banks are fully private entities competing in the market, they have their specific business model, which differs from commercial banks on some particular aspects (i.e. capital, governance and ownership). Therefore, we would like to stress that since IFRSs are designed for <u>all</u> types of companies, **a high standards setting process should also allow the maintenance of differences among business models** (i.e. cooperatives, partnerships etc.) and taking into account their accounting issues. We would detail this point in the context of the Monitoring Board as well (i.e. composition of the IASB).

Governance

How should the organisation best balance independence with accountability?

3. ***The current governance of the IFRS Foundation is organised into three major tiers: the Monitoring Board, IFRS Foundation Trustees, and the IASB (and IFRS Foundation Secretariat). Does this three-tier structure remain appropriate?***

4. ***Some stakeholders have raised concerns about the lack of formal political endorsement of the Monitoring Board arrangement and about continued insufficient public accountability associated with a private-sector Trustee body being the primary governance body. Are further steps required to bolster the legitimacy of the governance arrangements (including in the areas of representation of and linkages to public authorities?***

EACB thinks that the IFRSs Foundation have made some progresses in better involving stakeholders in the standards-setting process. EACB particularly appreciated the opportunity to express our members' views at organised roundtables on financial instruments during 2009-10. However, taking into account those communication efforts, we think that there is still room for improvement. In particular the IFRS Foundation remains a private organisation, which has been given the role of standards maker for all listed companies in the EU. Therefore, it is clearly important to ensure that the IFRS Foundation is committed to the public interest, whilst preserving the technical independence of the IASB (IFRS Foundation Secretariat).

EACB recommends better clarifying the place and role of each body of the there-tier structure. When doing so, it is important to differentiate between the need for independent high quality execution of standards and the need for a strong accountability framework:

- The IASB should improve the **participation of all relevant stakeholders** in the standard-setting process (including relevant supervisory authorities, see our response above). It should introduce the use of impact assessment and communicate on the reasons for changing accounting standards at an earlier stage of the standards-setter process in order to achieve greater transparency about technical choices made. In this respect, we would appreciate a work program discussed through an annual <u>public</u> consultation (see our responses to questions 5 & 6).

- The Trustees should continue their a**ssessment of the IFRS Interpretation Committee**. They should ensure that the appointment procedure of the Board's members is transparent and due account in taken of the interest of various interest groups. The Trustees should continue their roles of raising funds for the Foundation as well. Moreover, we would recommend the Trustees to develop its oversight activities further and communicate appropriately on the process and outcome of that oversight to its stakeholders.

- The **governance role of the Monitoring Board** should consist of designing the mission, fundamental structure, composition and due process of the IFRS Foundation and overseeing that it is functioning as anticipated. We would recommend improving the composition of the Monitoring Board as well: it should not be limited to public authorities responsible for setting financial reporting in capital markets. In particular, it should be extended to the Basel Committee.

EACB generally supports more transparency in the nomination process of the members of those three structures. In fact, we believe that enhancing the geographical and sector balance in particular within the IASB would calm concerns on legitimacy and provide more credibility to the standards setter.

We would take the opportunity to express our detailed views on the matter within the ongoing consultation of the Monitoring Bard.

Process

How should the organisation best ensure that its standards are high quality, meet the requirements of a well functioning capital market and are implemented consistently across the world?

5. ***Is the standard-setting process currently in place structured in such a way to ensure the quality of the standards and appropriate priorities for the IASB work programme?***

6. ***Will the IASB need to pay greater attention to issues related to the consistent application and implementation issues as the standards are adopted and implemented on a global basis?***

EACB supports the steps made by the IASB to allow stakeholders to express their views during the standard-setting process. As stated above, we particularly appreciate the opportunity to participate in roundtables with the IASB. Therefore, we would particularly recommend the IASB to organise further such meetings with stakeholders. Moreover, we suggest the following for further improvements:

- We believe that the **IASB's technical agenda-setting could be more consultative**. We would welcome that the IASB begins its deliberations on the future agenda by launching an annual public consultation process as requested by many other constituents. That would highlight potential needs and avoid possible criticisms on the relevance of the review of standards that do not cause any significant concerns in practice. Moreover, it would notably avoid the future IASB agenda being as congested as it has been recently. In this respect, we urge that sufficient time comment periods should be retained in order to give us adequate time to assess new proposals in detail and be able to provide high level inputs (i.e. we would like to refer to the short comment period of 60 days the IASB decided for the supplement to the exposure draft on impairment of financial instruments). Generally, we think that the IASB should never rush when reviewing/adopting IFRSs. Like EFRAG, we do not support the June 2011 deadline. We agree that it has become artificial and find the prevalence of any artificial deadlines on high quality standards damaging. Equally, we fear that standards finalised under heavy time pressure may give rise to more changes in the later period either by IFRS interpretations or revisions of the standards.

- The IASB should foresee sufficient resources to understanding the **impact of proposals prior to the issuance of Exposure Drafts**, giving greater consideration of the number of amendments that users and preparers of financial information can reasonably absorb within certain timeframes. As an illustration, we would like to recall our strong concerns on the piecemeal approach retained by the IASB to review IAS 39. Equally, we do not feel comfortable with the decision taken to issue a first part of the IFRS 9 at the end of 2009 with a mandatory date of application in 2013 (see our comments on adequate time for implementation below). Banks definitely need more time to assess all the consequences (expected to be huge) of the application of the new IFRS 9 from a management perspective as well as regarding the internal processes, IT systems, personal training etc.

- EACB members would equally appreciate that the IASB performs a **systematic field-testing of the proposals**. Moreover, we think that conclusions would have been published before the standards are formally issued.

- As we stated above mentioning the IFRS 9 example, EACB members underline that an **adequate time for implementation of standards** is of main importance. Generally, stakeholders should not be faced with frequent and huge changes to standards.

- The IASB should carry out **post-implementation reviews** of at least the major standard-setting projects (i.e. on financial instruments) as well to ensure that there are no significant interpretation and implementation issues. Those impact assessments should allow the evaluation of the practical effects of the future standards rather than interpreting the consequences of abstract concepts. Moreover, EACB asks the IASB to continue to ensure that its proposed standards are clear and comprehensible as well as capable of being implemented and audited in a practical manner.

- Furthermore, our members reiterate their concerns when the Board motivates changes to standards as improvements while these changes obviously deal with the Conceptual Framework. Actually, we believe that **fundamental changes to IFRS should first be debated at a conceptual level**. It would allow consistency of accounting principles within accounting standards. We would mention as examples the equity definition when reviewing the IAS 32 (a topic that is particularly relevant for co-operative banks) and the content of profit and loss and other comprehensive income as an increased number of items are recorded in the OCI.

- EACB members strongly support the joint effort that the IASB and the FASB undertook to achieve a single set of high-quality global accounting standards. We recognise the efforts made by the boards to achieve **convergence of IFRSs and US GAAP** and the difficulties they meet. However, again the “financial instruments” project is a good example. While we are aware that the Boards have to deal simultaneously with all the complex aspects of accounting for financial instruments in a very short time frame, we have strong concerns as regards the lack of coordination between the boards on the matter. We noticed the inconsistency between the FASB’s tentative decisions and the IASB’s. In particular, assessing FASB proposals in September 2010 (almost one year after the IASB has issued its IFRS 9) it became evident that the FASB approach would differ significantly from the IASB’s IFRS 9.

Financing

How should the organisation best ensure forms of financing that permit it to operate effectively and efficiently?

7. Is there a way, possibly as part of a governance reform, to ensure more automaticity of financing?

EACB thinks that stable and diversified funding is crucial for the independence of the IASB. It would notably provide jurisdictions using IFRSs with a greater assurance on the quality and the independence of the accounting standards. In that respect, we took note of the recent decision for the European Commission to contribute to the Foundation and that National Funding Mechanisms have been set up in some European jurisdictions.

End.