

**Charlie McCreevy**

European Commissioner for Internal Market and Services

## **Striving for a Single European Market - The role of accounting**

~~Check Against Delivery  
Seul le texte prononcé fait foi  
Es gilt das gesprochene Wort~~

Congress of German Public Auditors

**Berlin, 7 November 2007**

Dr Kämpfer, Ladies and Gentlemen,

It is a pleasure for me to be here with you today to discuss the vital role played by accounting and auditing in developing a single European capital market. As you may know, I am a chartered accountant by training, so these are issues very close to my heart. Now, as the Commissioner with responsibility for this area, I am convinced that the EU can deliver a significant contribution in helping businesses in Europe to become more competitive in today's global market.

## **Accounting**

A cornerstone for building an integrated single European capital market is the system of accounting standards. For companies to be able to raise capital throughout Europe, and for investors to compare company performance across borders, we need a common reporting language. Some years ago the EU set the course for building an integrated European capital market. We had come to a point where our financial reporting practices no longer met the new requirements for integrated markets. We had to rethink our approach. Finally, we decided to move to International Accounting Standards. That move was bold and visionary.

The changeover to IFRS did not come easy. It took a huge effort from our listed companies, auditors and regulators to adapt to the new accounting environment.

Now, more than two years later we can look back and see how it has gone. A number of studies have been carried out on the first year of IFRS implementation. One of them was issued very recently – that undertaken by the Institute of Chartered Accountants of England and Wales (ICAEW) at the request of the Commission. This study concludes that IFRS implementation has been "challenging but successful". Other studies, including the one issued by CESR on the first year of enforcement, convey the same message. Research also shows that the overall quality of accounts and disclosures have improved and that the changeover to IFRS has been achieved without disturbance to the market.

Of course, this does not mean that we don't still have work to do. The introduction of 40 new standards has given rise to some issues surrounding application and interpretation. Some of the standards had inconsistencies, and there were some areas which were not covered by reporting standards. As regards the application of standards, some issuers still had room for improvement in providing sufficient disclosures. However, overall the news is very positive – we are on the right track. Accounting is making a significant contribution to the building of a single European capital market.

## **Global accounting standards**

Building the European capital market is important. But the game increasingly has to be played in the global arena. The transatlantic capital market is by far the biggest market worldwide and the EU-US relationship is very special. I am very pleased that the roadmap which I have been working on together with my US colleague, Chairman Cox of the SEC, is now about to deliver. US GAAP and IFRS are converging. And the SEC has presented a proposal to allow foreign issuers to file accounts under IFRS without reconciliation to US standards. We are still working on some details to ensure that proposal is of the greatest possible benefit to EU issuers in the US – I am visiting the US tomorrow and Friday. But I am very confident that the objective: to be able to harvest the benefits of friction-free transatlantic capital markets – is within our grasp.

As IFRS are becoming the global standard the time is ripe to address the issue of the governance and the accountability of the International Accounting Standards Board – the IASB. Today, a number of authorities responsible for the regulation of the world's capital markets, including the Financial Services Agency of Japan, the International Organization of Securities Commissions (IOSCO), the US Securities and Exchange Commission and the European Commission are proposing changes to strengthen the institutional framework of the IASB and the International Accounting Standards Committee (IASC) Foundation to make them more accountable to those governmental authorities charged with the protection of investors and the regulation of capital markets. In the coming months all concerned should devote their energies to make sure the IASB becomes more accountable while preserving its independent nature and that it continues to improve its due process with state of the art impact assessments, feed-back statements and public consultations.

## **Auditing**

The application of International Financial Reporting Standards is crucial for the business community at large. Accounting is not only pivotal for investors in our capital markets. It can also be the key for access to finance for the entire economy. It is through high quality audits that investors in Europe get the reasonable assurance that the accounts provide a true and fair view of the company's financial position. In Europe, we moved to new legislation on statutory audit in 2006, with the Eighth Company Law Directive.

The Directive represents a sea change for the audit profession. We needed the Directive to improve audit quality and to restore public confidence in the audits in Europe. In the past, a few rotten apples poisoned the whole applecart of public good. So political agreement on the way forward was reached in Brussels in 2006. Today, we must ask ourselves: are we delivering what we agreed upon?

### **1. Implementation of the Directive – a job for Member States**

I have been asked to talk about the issues the Commission is working on. But the focus should also be on what Member States are doing or *should* be doing. They have a major job on which they have to deliver. We can assist, we can inform, but it is for Member States to implement the Directive into national law. They also have to establish an effective public oversight because the Directive requires them to do so.

By June 29<sup>th</sup> 2008, all Member States should have notified their implementation measures to the Commission. We shall monitor the situation closely. This will not be a box-ticking exercise. The transposition of this directive will have a direct impact on audit quality in the EU. We want it to restore confidence in the audit profession. We shall work closely with Member States in the next eight months to make sure that together we can achieve these goals.

The German law on reforming public oversight and inspections entered into force in September 2007. But other changes to independence rules and to how networks should be defined are not yet enacted. It is therefore important that the framework is completed.

## **2. Organising Public oversight – a job for Member States**

One element of this overhaul of auditing regulation is the establishment of effective public oversight. This oversight is essential in improving audit quality by strengthening public confidence in auditing. This is a challenge for all our Member States. It is not enough for them to write a law providing for the establishment of an oversight system. We need an *effective* oversight in all 27 Member States. Germany has made commendable achievements in this regard. I recognise that the practical implementation is not always an easy ride for all parties. But independent oversight under the new Directive will mean that the times of self-regulation are over.

Not all Member States are as advanced as you are in Germany. The European Union should work on the basis of "home country oversight" from June 2008. Will we be ready? My services will work closely with all Member States to ensure that we are. If necessary we might consider using peer pressure mechanisms to motivate laggards.

## **3. The role of the Commission**

The Commission is assisting the domestic process by promoting co-ordination of public oversight bodies at European level. The European Group of Auditor Oversight Bodies plays an important role in this regard. A European group where national oversight bodies come together regularly is an important asset to ensure coherent approaches in all jurisdictions. The Commission chairs this European Group and ensures that they meet regularly with representatives from the profession.

As a result of the discussions amongst public oversight bodies we are also working on the issue of the so-called "quality assurance". We want to give guidance to statutory auditors and audit firms on how to carry out high quality audits of listed companies. For other types of audits it would seem that the Directive already provides a sufficient set of principles and that there would be no need for further recommendations. Obviously, we have also involved the audit profession in our deliberations.

The 8<sup>th</sup> Directive also addresses the question of what to do with audit firms from third countries. It empowers the Commission to assess the equivalence of the systems of public oversight in third countries. If deemed equivalent, Member States would not need to carry out the oversight of foreign audit firms themselves but could rely on the third country oversight. We are discussing this issue with all those concerned. As regards US firms my colleagues have had numerous meetings with the US PCAOB. PCAOB Chairman Mark Olson as well as Charles Niemeier have been important driving forces in this process. Now both the EU and the US should seize this unique opportunity and agree on a common framework for co-operation. For the benefit of audit firms, companies and the financial services industry, we cannot afford failure.

## **4. New issues**

Let me turn now to some upcoming issues.

At a global level, a number of ideas on the future of the audit profession are on the agenda. In June this year, the International Organisation of Securities Commissions (IOSCO) organised a round table in Paris in this regard. In the US, Treasury Secretary Paulson set up an advisory committee in October which is expected to provide recommendations by summer next year.

In the same vein, my services have recently published the results of an independent study analysing the impact of ownership rules of audit firms. Since this is a global issue it requires global solutions. Therefore, we shall continue to contribute to the debate in close co-operation with other jurisdictions and international organisations.

Then there is the issue of auditor liability. In Germany, a cap on liability has existed since 1931 and nobody in Germany seems to feel that this undermines audit quality. In Europe we are still debating on this question.

And finally I would like to mention the International Standards on Auditing or ISA's. We are currently considering the merits of introducing ISAs in Europe. Before the end of this year, my services will launch a study on the costs and benefits of introducing ISA's as well as any potential differences with US standards. Once we have some results we shall be able to reassess the situation.

## **Simplification**

We should not limit ourselves to looking at possible new rules and projects at EU level. We also need to ask ourselves the question whether what we already have in place is still up to the needs of today's business. And in my view for many of the rules that we have in accounting, auditing and company law in general this is not the case. This is why the Commission adopted a Communication in July that sets out its proposals for simplifying the business environment for companies and in particular for reducing administrative burdens for SMEs. We shall of course stick to our objective of maintaining and improving the high accounting and auditing quality in the EU. But some of the existing requirements might entail administrative work that some companies, in particular small and medium-sized ones, find unnecessarily burdensome. Less administrative burden and less red tape will help European business to become more competitive in today's global markets.

## **Conclusion**

In conclusion, ladies and gentlemen, we have come a long way in creating an appropriate framework in which accounting, auditing and company law rules can play a decisive role in shaping the future of Europe's capital markets. Much remains to be done, especially at Member State level, and this is where the focus of attention should now shift. But equally, with today's increasingly interconnected global markets, it is imperative that we drive forward to seize the opportunities that international cooperation can afford us. For the benefit of Europe's auditing industry, companies and investors, Europe has to be in the driving seat, not bringing up the rear.

Thank you.