

Press Release

28 July 2009

Financial Crisis Advisory Group publishes wide-ranging review of standard-setting activities following the global financial crisis

The Financial Crisis Advisory Group (FCAG), a high level group of recognised leaders with broad experience in international financial markets, today published its recommendations related to accounting standard-setting activities, and other changes to the international regulatory environment following the global financial crisis.

The FCAG was formed at the request of the International Accounting Standards Board and the US Financial Accounting Standards Board to consider financial reporting issues arising from the crisis. Co-chaired by Hans Hoogervorst, Chairman, AFM (the Netherlands Authority for the Financial Markets) and Harvey Goldschmid, former Commissioner, US Securities and Exchange Commission, the FCAG met six times from January to July 2009.

The report of the FCAG articulates four main principles and contains a series of recommendations to improve the functioning and effectiveness of global standard-setting.

The chief areas addressed in the report are:

1. Effective financial reporting
2. Limitations of financial reporting
3. Convergence of accounting standards
4. Standard setter independence and accountability

The principles and a summary of the recommendations are set out in the appendix to this press release. The FCAG will reconvene in December to review the progress made on its recommendations.

Commenting on the report, Hans Hoogervorst, Co-Chairman of the FCAG said:

I urge policymakers around the world to study the report and to take note of its conclusions, especially the importance of broadly accepted accounting standards that are the result of a thorough due process. The report highlights the importance but also the limits of financial reporting. Accounting was not a root cause of the financial crisis, but it has an important role to play in its resolution.

Harvey Goldschmid, Co-Chairman of the FCAG added:

As our report emphasizes, improved financial reporting will help restore the confidence of financial market participants and thereby serve as a catalyst for increased financial stability and sound economic growth. The independence and integrity of the standard-setting process, including wide consultation, is critical to developing high quality, broadly accepted accounting standards responsive to the issues highlighted by the crisis. It's been a great pleasure to work with Hans Hoogervorst and the other distinguished members of the Financial Crisis Advisory Group.

The report of the FCAG can be downloaded from <http://go.iasb.org/fcag> or <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1175801889213>.

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Notes for editors

About the FCAG

The composition of the FCAG is as follows:

Co-Chairman

- **Harvey Goldschmid**, former Commissioner, US Securities and Exchange Commission
- **Hans Hoogervorst**, Chairman, AFM (the Netherlands Authority for the Financial Markets)

Members

- **John Bogle**, Founder, Vanguard, United States
- **Jerry Corrigan**, Goldman Sachs and former President of the New York Federal Reserve Bank, United States
- **Fermin del Valle**, former President, IFAC, Argentina
- **Jane Diplock**, Chairman, IOSCO Executive Committee, New Zealand
- **Raudline Etienne**, Chief Investment Officer, New York State Common Retirement Fund
- **Stephen Haddrill**, Director General, Association of British Insurers, UK
- **Toru Hashimoto**, former Chairman, Deutsche Securities Limited, Japan
- **Nobuo Inaba**, former Executive Director, Bank of Japan, Japan
- **Gene Ludwig**, former Comptroller of the Currency, United States
- **Yezdi Malegam**, Board Member, Reserve Bank of India, India
- **Klaus-Peter Müller**, Chairman of the Supervisory Board, Commerzbank, Germany
- **Don Nicolaisen**, former Chief Accountant, US Securities and Exchange Commission, United States
- **Wiseman Nkuhlu**, Chairman of the Audit Committee, AngloGold Ashanti; former Economic Advisor to the President of the Republic of South Africa
- **Tommaso Padoa-Schioppa**, former Finance Minister, Italy
- **Lucas Papademos**, Vice-President, European Central Bank
- **Michel Prada**, former Chairman, Autorité des marchés financiers, France

Observers:

- **Basel Committee of Banking Supervisors**
- **Committee of European Securities Regulators**
- **International Association of Insurance Supervisors**
- **Japan Financial Services Agency**
- **US Securities and Exchange Commission**
- **Nelson Carvalho**, former Chairman, IASB SAC, Brazil
- **Dennis Chookaszian**, Chairman, FASAC, United States

VI. Restatement of Principles and Recommendations

Principle 1: Effective financial reporting

Financial reporting plays an integral role in the financial system by striving to provide unbiased, transparent and relevant information about the economic performance and condition of businesses. Effective financial reporting depends on high quality accounting

standards as well as the consistent and faithful application and rigorous independent audit and enforcement of those standards.

Financial reporting is of great importance to investors and other financial market participants in their resource allocation decisions and to regulators and other users. The confidence of all these users in the transparency and integrity of financial reporting is critically important to global financial stability and sound economic growth.

Where regulatory standards differ from accounting standards in ways that could have significant effects on financial reporting, the effects of those differences should be disclosed in a manner that does not compromise the transparency and integrity of financial reporting.

Recommendations

- 1.1. The Boards should give highest priority to their project to simplify and improve their standards on financial instruments, moving forward as a matter of urgency but with wide consultation.
- 1.2. Recognizing that in some areas, such as impairments, IFRS and US GAAP have different starting points, we nevertheless urge the two Boards to achieve converged solutions.
- 1.3. In the financial instruments project, the Boards should explore alternatives to the incurred loss model for loan loss provisioning that use more forward-looking information. These alternatives include an expected loss model and a fair value model.
- 1.4. If the Boards pursue an expected loss model, care must be taken to avoid fostering “earnings management,” which would decrease transparency.
- 1.5. In the financial instruments project, the Boards should reconsider the appropriateness of an entity’s recognition of gains or losses as a result of fair value changes in the entity’s own debt because of decreases or increases, respectively, in its creditworthiness.
- 1.6. Accounting standards, especially on financial instruments, consolidation/derecognition and risk disclosure, have special importance for prudential regulators. Accordingly, it is important that the Boards continue their consultation with prudential regulators.
- 1.7. If an alternative to the incurred loss model is developed that uses more forward-looking information, it may well narrow the differences between the requirements of accounting standards and of regulatory standards. To the extent differences remain, we urge the Boards to develop a method of transparently

depicting any additional provisions or reserves that may be required by regulators without undermining the integrity of financial reporting by affecting income statement-based metrics.

- 1.8. While giving priority to the financial instruments project, we also strongly urge the Boards to make substantial progress on converged and improved standards on consolidation and derecognition (i.e., on off-balance sheet issues) and the other areas within their Memorandum of Understanding.
- 1.9. In the meantime, the FASB's new off-balance sheet standards should be implemented without revision or delay.
- 1.10. In the financial instruments and consolidation/derecognition projects, improvements should be made with an eye toward a better, more transparent depiction of the risks involved, especially with complex financial instruments.

Principle 2: The limitations of financial reporting

Although effective financial reporting provides indispensable rigor and transparency to the market, investors, analysts, regulators and others cannot rely exclusively on the information it provides. All users should recognize the limitations of financial reporting: it provides only a snapshot in time of economic performance, and cannot provide perfect insight into the effects of macro-economic developments. Financial reporting is also dependent on the generation of reliable data by well-functioning markets that have proper infrastructure, and the use by financial institutions and other business entities of proper processes for price verification and other aspects of the valuation of assets and liabilities.

Recommendations

- 2.1. In their joint conceptual framework project, the Boards should clearly acknowledge the limitations of financial reporting.
- 2.2. Users of financial reporting should recognize its limitations and should never suspend their own judgment and due diligence.
- 2.3. We urge the appropriate authorities to ensure that all over-the-counter markets, especially those for structured products and derivatives, have robust infrastructure that fosters the transparency of market prices.
- 2.4. Business entities, especially financial institutions, should employ effective price verification processes and otherwise improve their valuation of assets and liabilities. For price verification to be most reliable, these functions should, wherever possible, be completely independent of sales, trading and other commercial functions.

Principle 3: Convergence of accounting standards

Because of the global nature of the financial markets, it is critically important to achieve a single set of high-quality, globally converged financial reporting standards that provide consistent, unbiased and transparent information, regardless of the geographical location of the reporting entity.

Recommendations

- 3.1. We strongly urge the Boards, consistent with the need for maintaining and enhancing high quality accounting standards, to use every effort to achieve converged solutions. This should be done in the projects that they have accelerated in response to the financial crisis (financial instruments and consolidation/derecognition) and in the other projects covered by the Boards' Memorandum of Understanding.
- 3.2. We urge national governments, financial market participants, and the global business community to support actively the development of a single set of high-quality accounting standards.
- 3.3. To sustain momentum, we encourage all national governments that have not already done so to set a timetable that is both practicable and firm for adopting or converging with IFRS.
- 3.4. Even if accounting standards are converged, differences in financial reporting may arise from differences in national or regional auditing standards, or differences in enforcement. We urge the appropriate international organizations to take note and reach converged solutions and common interpretations that will harmonize with those of the accounting standard setters. We believe international accounting firms can play a particularly important role in this regard.

Principle 4: Standard setter independence and accountability

To develop standards that are high quality and unbiased, accounting standard setters must enjoy a high degree of independence from undue commercial and political pressures, but they must also have a high degree of accountability through appropriate due process, including wide engagement with stakeholders and oversight conducted in the public interest.

Recommendations

- 4.1. The joint and comprehensive financial instruments project now underway should be the focus and chief priority of both Boards for the balance of 2009. In conducting this project, the Boards

should not compromise their due process procedures. We have committed to review the progress made by the Boards before year-end. We believe it is of critical importance that neither business nor political pressures divert the accounting standard setters from the financial instruments project, which is so important to the global financial system.

- 4.2. To ensure the widespread acceptance of its work in urgent situations, the Boards should define in advance the circumstances under which it is appropriate to act on the basis of expedited due process. The Boards should also develop procedures to ensure that, in such circumstances, the maximum consultation practicable is obtained
- 4.3. While, as part of the system of public accountability, policymakers can and should voice their concerns and provide input to standard setters, we urge them to refrain from seeking to prescribe specific standard-setting outcomes. Such restraint is important in maintaining public confidence in the independence of the standard setting process, and, thus, in financial reporting and the financial system as a whole.
- 4.4. To protect its independence from undue influence, the IASB must have a permanent funding structure under which sufficient funds are provided to it on an equitable and mandatory basis.
- 4.5. To bolster the authority of the Monitoring Board, its composition should be broadened geographically to include securities regulators from a wider range of nations.