

# U.S. Financial Accounting Standards Board

## A Discussion with our Korean Colleagues

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The views expressed in this presentation are my own and do not necessarily represent official positions of the Financial Accounting Standards Board. Official positions of the FASB Board are arrived at only after extensive due process and deliberations.

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## Topics for Discussion

- Background on the U.S. Financial Reporting System and the FASB
- International Convergence — A U.S. Perspective
- The “Principles versus Rules” Debate

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## Background on the U.S. Financial Reporting System

- Accounting Standards
  - FASB — public companies, private companies, not-for-profit entities
  - GASB — state and local governments
  - FASAB — U.S. federal government
- Auditing Standards and Inspection
  - PCAOB — public companies
  - AICPA — private companies
  - Others
- Key Role of the SEC
  - Regulation of the capital markets
  - Enforcement
  - Disclosure and reporting requirements
  - Oversight of FASB and PCAOB
- Current SEC reconciliation requirements for foreign registrants

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## Some Facts about the FASB

- Our Funding
- Our People
  - Seven Board members
  - Approximately 70 staff
- Our process — open, thorough due process with exposure drafts and other documents issued for public comment
- Emerging Issues Task Force (EITF)
- Many formal and informal advisory and liaison groups

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## FASB Strategic Objectives

- Improvement of U.S. GAAP
- Simplification
- International Convergence

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## A U.S. Perspective on International Convergence of Accounting Standards

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## Why Is U.S. Interested in International Convergence?

- Increasing Cross-Border Investing and Capital Flows
- Calls by Investors, Multinational Companies, and Large Auditing Firms, and others (Small Business/US Domestic Only Companies Less Enthusiastic)
- “Pax Americana” in Financial Reporting unlikely
- But to be Truly International Must Include U.S.
- Better U.S. Reporting

Summary:

Global Capital Markets Imply Global Standards

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## Official Encouragement

- FASB and SEC were very Supportive of Global Standard Setting at time of IASC Restructuring
- Sarbanes-Oxley Act
- SEC Policy Statement on FASB and SEC Report to Congress on “Principles-Based” Accounting
- SEC “Roadmap”
- Forthcoming SEC proposals on:
  - Possible Elimination of the Reconciliation Requirement
  - Possible Adoption of IFRS in U.S.

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## The Convergence Process

- The IASB's International Partnership
- The FASB-IASB Norwalk Agreement
  - Agenda Alignment
  - Joint Projects on Major Topics
  - “Modified” Joint Projects
  - “Short-Term” Projects on Targeted Differences
- The February 2006 “Memorandum of Understanding”

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## Convergence Activities

- Current Joint Projects
  - Conceptual Framework
  - Acquisition Method Procedures and Non-Controlling Interests
  - Revenue Recognition
  - Financial Statement Presentation (With IASB/ASBJ/ UKASB)
  - Accounting for Leases
- “Modified Joint” Projects (Share-Based Payments, Liabilities vs. Equity, Insurance, Fair Value Guidance, Pensions and Other Post Employment Benefits)
- “Short-Term” Convergence Projects
  - FASB — changes to U.S. GAAP to converge with IFRS
  - IASB — changes to IFRS to converge with U.S. GAAP
  - Both — changes to certain respective standards
- In Research Stage (Consolidations, Financial Instruments, Intangibles)

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## Challenges to Convergence

- Starting from Very Different Places (IASB, FASB, Other Countries)
- Significant Cultural, Institutional, Regulatory, and Legal Differences
- Agenda Misalignment
- Getting Boards to Agree
- Convergence vs. Improvement
- Principles vs. Rules

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## Challenges to Convergence Cont'd

- Pace of Change
- Constituent Reactions/Willingness to Change/Change Management
- Politics
- IASB Funding and Staffing
- Consistency of IFRS implementation — “as adopted” versions and national “flavors” of IFRS
- Effect of Eliminating the SEC reconciliation requirements on further convergence and improvement of accounting standards

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## In Summary

- FASB Committed to Working Towards Convergence
- Significant Resources Devoted to this Effort
- Convergence Considerations Embedded in our Process
- Not Just Convergence for Sake of Convergence — Better Reporting
- Making Slow but Steady Progress
- Convergence is a Process and a Destination
- Mutual Recognition versus Convergence?

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## The “Principles versus Rules” Debate

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## What Do We Mean by “Principles”?

- Ten Commandments — are they “principles” or “rules”
- “Concepts” versus “Principles”
- “Outcomes”/“Objectives” versus “Principles”

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## Then What is a “Principles-Based” Standard?

- Principles Derived from Concepts?
- Outcomes or Objectives Oriented?
- No rules?
- No exceptions?
- No bright lines?
- Short
- How much guidance/interpretation is necessary?
- My view

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## Can it work in U.S?

- Maybe
- “Rules-based” approach is a more pervasive issue in U.S. than just financial reporting
- But is this the right debate?

What do investors/users want?

What produces better financial reporting?

What are the costs and benefits of different systems?

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## What Would It Take to Make a “Principles-Based” Approach Work in the U.S.?

- Agreement on what it means
- More agreement that it would improve financial reporting
- Significant institutional, structural, cultural, and behavioral changes by many parties
- Concerted and coordinated efforts to address forces that create and reinforce “rules-based” thinking and behavior in our system

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## Who Would Need to do What?

- Standard-setters?
  - What has the FASB been doing?
- Preparers?
- Auditors?
- Boards/Audit Committees?
- Regulators/Enforcers?
- Media?
- Investors/Users
- Accounting and Auditing Educators and CPA Exam
- Legal System?

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## Some Other Observations/Considerations

- Impact of debates about:
  - Purpose of financial reporting (decision-usefulness versus stewardship)
  - “Relevance” versus “Reliability”
  - Measurement in Accounting
- Impact of Technology (XBRL, etc.) on Financial Reporting

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## Some Final Thoughts

- The key goals should be both improvement and convergence
- Convergence to high quality global reporting will also require changes and local improvement in other areas including auditing and regulatory review and enforcement
- It's a big world – key is to continue the dialogue and discussion, listening and learning from others.

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