



**CESR's technical advice on a mechanism for  
determining the equivalence of the generally  
accepted accounting principles of third countries**

30 May 2007



**INDEX**

**I. EXECUTIVE SUMMARY ..... 3**

**II. INTRODUCTION..... 4**

**III. MECHANISM FOR DETERMINING EQUIVALENCE..... 6**

## I. Executive summary

1. CESR provides in this advice a mechanism for determining equivalence of the generally accepted accounting principles of third countries to IFRS as adopted in the EU (summarized in the form of a chart in appendix one). The main elements of the proposed mechanism are outlined in the paragraphs below.
2. The national standard setter (and/or another suitable public body) should assess whether the disclosures, measurement and recognition principles, and financial statement presentation required by the third country GAAP concerned are materially the same as IFRS and where they are not an assessment of the differences.
3. If there are no significant differences between the third country GAAP and IFRS (for example because a convergence programme has reached a point where no material differences exist any more), such GAAP may be deemed equivalent without the need for additional rectification disclosures.
4. Even in cases where there are significant differences under the two sets of accounting principles, the third country GAAP may be considered equivalent to IFRS if those differences identified can be rectified at company level by non-complex disclosures.
5. Any additional non-complex disclosures should be subject to audit.
6. Prior to giving any advice to the Commission on whether to accept an equivalence assessment, CESR would seek reactions from market users regarding the third country GAAP and the proposed rectifications via public consultation.
7. An "overall" assessment of equivalence should be made in the final instance by the European Commission via a comitology process once all other steps have been fulfilled and using the definition of equivalence CESR has already provided.
8. For the purposes of establishing equivalence, CESR assumes that third country GAAPs are properly applied including the provision of any rectifying disclosures necessary. CESR further assumes that the necessary filters for ensuring market confidence are in place for third country issuers using or participating in the EU capital markets.
9. Finally, CESR considers that an assessment of the reliability of the audit conducted on the financial statements of issuers using an equivalent GAAP should be a step in the mechanism. The assessment of the audit filter is dealt with exclusively through the assessment of compliance with the 8<sup>th</sup> Directive<sup>1</sup>, including any transitional measures the European Commission may introduce.
10. In addition to its proposed mechanism for determining equivalence, CESR suggests the European Commission considers extending the existing transitional measures for those GAAPs currently converging to IFRS if certain conditions are met. Should the Commission adopt such transitional measures, CESR would recommend they not be extended beyond 2012.

---

<sup>1</sup> DIRECTIVE 2006/43/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC

## II. Introduction

### Background

11. The Prospectus Directive and Regulation (“the prospectus regime”)<sup>2</sup> and the Transparency Directive<sup>3</sup> will require the European Commission (“EC or the Commission”) to establish by mid 2008 whether a given third country GAAP is equivalent to IFRS<sup>4</sup>.
12. As a result of the prospectus regime, third country issuers who have their securities admitted to trading on an EU regulated market or who wish to make a public offer of their securities in Europe, are required from 1st January 2007 to publish a prospectus including financial statements prepared on the basis of EU endorsed IFRS or on the basis of a third country’s national accounting standards (third country GAAP) if these standards are equivalent to endorsed IFRS. From the period 1 January 2007 until 31 December 2008, appropriate transitional arrangements apply under Article 35 of the Commission Regulation on prospectuses.
13. Similarly, under the Transparency Directive, from January 2007 third country issuers whose securities are admitted to trading on an EU-regulated market will also have to provide annual and half-yearly financial statements which should either be prepared in accordance with IFRS or third country GAAP equivalent to endorsed IFRS. Appropriate transitional arrangements also apply under Article 26 (3) of that Directive.
14. In December 2006 the EC adopted two measures<sup>5</sup> allowing a two-year transitional period (until January 2009) during which third country issuers can prepare their annual financial statements and half-yearly financial statements in accordance with the accounting standards of Canada, Japan or the United States. The aim of these transitional provisions was to give more time to the standard setters and regulators of those countries to continue with their convergence processes. As other countries are also in the process of converging their national GAAPs to IFRS over various periods of time, the Commission considered it appropriate to allow the same two-year transitional period for these third country issuers to continue preparing their annual and half-yearly financial statements in accordance with a GAAP that is converging to IFRS, provided certain conditions are met.
15. The abovementioned December 2006 measures envisage a different treatment of third country issuers before and after January 2009:
  - Transitional period until January 2009. During this phase, accounting frameworks other than IFRS, Canadian, Japanese or US GAAP may be used subject to certain conditions<sup>6</sup>. The decision to accept other accounting frameworks is the responsibility

---

<sup>2</sup> Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC

Commission Regulation (EC) No 809/2004 of 29 April 2004 implementing Directive 2003/71/EC of the European Parliament and the Council as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements.

<sup>3</sup> Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.

<sup>4</sup> The term “IFRS” should be understood in this paper as referring to IFRS as adopted by the EU.

<sup>5</sup> Commission Regulation 1787/2006 of 4 December amending Commission Regulation 809/2004 on prospectuses and Commission Decision 2006/891/EC of 4 December 2006 on the use by third country issuers of securities of information prepared under internationally accepted accounting standards (“the Transparency Decision”).

<sup>6</sup> According to the revised Article 35.5A (c) of the Prospectus Regulation (and the similar provision in the Transparency Decision) these conditions are:



of the competent authority, although recitals in the two measures state that *“To ensure consistency within the Community, CESR should co-ordinate the competent authorities’ assessment as to whether those conditions are satisfied in respect of individual third country GAAP”*.

- After the transitional period, a third country’s GAAP will be acceptable only if it has been determined equivalent to IFRS by the European Commission pursuant to their definition of equivalence which they will establish by 1 January 2008. The Commission will consult CESR on the appropriateness of the definition of "equivalence", the "equivalence mechanism" and the actual determination of equivalence.
16. At least six months before 1 January 2009, the Commission shall ensure a determination of the equivalence of the GAAP of third countries, pursuant to a definition of equivalence and an equivalence mechanism that it will have established before 1 January 2008. In order to start the process for determining equivalence, the EC has asked CESR for advice in several phases. On March 2007 CESR submitted to the European Commission its first advice containing a definition of equivalence. This document now addresses the second element of this process namely advice on establishing a mechanism for determining equivalence.
  17. Once CESR has provided its advice, the Commission must by 31 December 2007 adopt a legal measure, via comitology, on the definition of equivalence and the determination of equivalence (in accordance with article 35.5E of the Prospectus Regulation and article 2.5 of the Transparency Decision).
  18. Within CESR, the operational group CESR-Fin chaired by Paul Koster, Commissioner of the Netherlands Authority of Financial Markets (AFM) has been charged with fulfilling the EC’s request.
  19. CESR published a consultation paper on 17 April 2007 to seek input from market participants on its proposals for a mechanism for determining equivalence. Specific questions were asked in certain areas where CESR was considering different policy options. CESR has received 17 responses which can be viewed on its website. In addition to containing advice to the Commission, this paper also discusses CESR’s reaction to the main comments raised by the consultation’s respondents (paragraphs referring to respondents’ comments and CESR’s reactions to those comments are in italics).

- 
- (i) The third country authority responsible for the national accounting standards in question has made a public commitment, before the start of the financial year in which the prospectus is filed, to converge those standards with IFRS;
  - (ii) That authority has established a work programme which demonstrates its intention to progress towards convergence before 31 December 2008; and
  - (iii) The issuer provides evidence that satisfies the competent authority that the conditions in (i) and (ii) are met.

### III. Mechanism for determining equivalence

#### *Extract of the Commission's mandate*

The Commission requests CESR to advise on a suitable mechanism for determining the equivalence of a third country GAAP. This is not an assessment of which GAAPs are equivalent, but of the mechanism, or procedure, for making that assessment. CESR is asked to provide advice on these matters by 1<sup>st</sup> May 2007.

#### *Application - Comparison of disclosures and measurement principles*

20. The process for determining equivalence should be initiated by an application to the European Commission by the standard setter of the jurisdiction seeking equivalent status of its accounting principles or/and another public organisation from the country of origin of the issuer (e.g. a securities or another financial supervisor from the third country or its ministry of finance) or from a Member State or a public body from a Member State such as a CESR member in the case described in paragraph 12.
21. The application should include an honest assessment of whether the disclosures, measurement and recognition principles, and financial statement presentation required by the third country GAAP concerned are materially the same as IFRS and where they are not an assessment of the differences. CESR considers that this assessment should be done in the first instance by the standard setter of the country seeking equivalence, as this body is in the best position to compare its own standards with IFRS. As discussed above, alternatively, or in cooperation with the standard setter, another body with public responsibilities could perform the task, as suggested by some respondents to the consultation.
22. *CESR sought views from market participants specifically on the case where a standard setter is not able or willing to initiate and substantiate an equivalence application. Some respondents suggested that in such situations it should also be possible for an issuer (or group of issuers) to make and substantiate such application. Whilst CESR acknowledges that it is the prerogative of the Commission to use its comitology powers and ask CESR for advice on the equivalency of which ever third country GAAPs it might deem appropriate, CESR sees difficulties in handling applications where the assessment of those GAAPs will be made solely by issuers and their advisors. Therefore, even if an application to the Commission could be made by individual issuers or groups of issuers, CESR considers that only those applications supported by one or more of the abovementioned public bodies should be accepted and further progressed. This would also mean that CESR would expect the preliminary assessment of the third country GAAP concerned to be performed by one of these organisations.*
23. *As indicated above, CESR considers that only public bodies are suitable to carry out the comparison of the local GAAP to IFRS. CESR's rationale for this is that public bodies, being suitably independent from issuers and other interested parties, are more likely to be in a position both to perform the task of initial assessment with appropriate dispassion and objectivity and to provide the subsequent on-going support to the assessment (as envisaged in paragraph 42).*
24. Regarding the comparison of measurement principles, CESR considers that it is only necessary that the third country GAAP principles be allowed under IFRS for these to be considered acceptable. Consequently, the principles concerned do not need necessarily to be the same as those an IFRS issuer might have chosen in the circumstances. This is in line with the spirit of a GAAP being equivalent not the same as IFRS.
25. CESR considers that the assessment of technical differences between the standards would be best performed as part of a convergence programme aiming at some later date to eliminate

such differences but this does not necessarily have to be the case. Consequently CESR believes a mechanism should be designed to operate independently of "convergence" or "adoption" programmes and does not assume that a third country GAAP must be involved in one of these to be found equivalent if adequate alternative remedies to align principles and disclosures can be identified. CESR believes this approach is conducive to the equivalence mechanism being as "fair" as possible to all third country issuers whilst still encouraging issuers from third countries who seek access to EU markets to progress towards the use of IFRS.

26. The degree of detail regarding the technical differences that standard setters should provide will vary a great deal depending on the nature of the GAAP concerned. However in the absence of any specific guidance on the level of information required, the level of detail included in CESR's 2005 assessment of the equivalence of the GAAP of Canada, Japan and the US (CESR/05-230b) is a good indication of the level of detail CESR would envisage the local standard setter's assessment providing.
27. *CESR specifically asked in the consultation paper whether it should publish guidance on the information it would consider satisfactory to ensure an informed assessment can take place. There were mixed views from market participants. Some considered that the 2005 advice should be the benchmark whilst others asked for high level guidance considering that the 2005 assessment of the GAAPs of Canada, Japan and the US was too detailed an exercise. Overall, CESR's view is that the level of detail required in the 05-230b 2005 advice is in general the appropriate one. Although individual circumstances will have to be taken into account, CESR does not see in principle a reason to discriminate between those three countries assessed in 2005 and those other countries who may now wish to make an application under the principles of the mechanism that CESR is recommending.*

#### ***Remedies for significant GAAP differences***

28. Even in cases where the standard setter identifies significant differences in the measurement and recognition principles or in the disclosure or presentation requirements under the two sets of accounting principles, CESR believes it is still possible for a third country GAAP to be considered equivalent to IFRS if those differences identified can be rectified at company level by non-complex disclosures (for example, the narrative explanations or the supplementary statements discussed in paragraphs 99 and 101-104 of CESR/05-230b 2005 advice). For the avoidance of doubt CESR envisages that such disclosures will be in the third country GAAP concerned and designed to rectify at GAAP level any significant differences to IFRS. Finally, it is worth mentioning that CESR does not consider even a full reconciliation to IFRS as satisfying the equivalency provisions as an appropriate remedy, for the reasons stated in its 2005 advice.
29. Any additional disclosure requirements for rectification of the target GAAP should again in the first instance be suggested by the standard setter of the country seeking equivalent status. These disclosures should not be so numerous or fundamental as to render the original accounts prepared by the issuer meaningless or too difficult to follow for an "informed private investor".
30. The suggestion that such additional rectification disclosures might be used to enable a third country GAAP to be considered equivalent to IFRS does not imply that such rectifications will always be necessary. A third country GAAP may already be based on or very close to IFRS or a previous convergence programme between the third country GAAP and IFRS might have reached a point where no significant differences are considered to exist any more. In all such cases a decision that no additional disclosures are required could legitimately be reached.

### ***CESR consultation and assistance to the EC***

31. The assessment required by the mechanism both of the appropriateness of the rectification disclosures and their non-complexity, should be performed by CESR before providing advice to the European Commission on the equivalence or otherwise of the third country GAAP being assessed. In order to inform its view prior to giving any such advice, CESR would expect to seek reactions from market users or other interested professional participants regarding the third country GAAP and the proposed rectifications via public consultation and direct consultation. CESR assumes that rational investors who invest in securities issued by third country issuers reporting under their local GAAP will have a reasonable knowledge of the GAAPs concerned and a reasonable idea of the major rectifications needed to give them the same level of investment relevant information as a set of IFRS accounts. Accordingly, CESR's assistance to the Commission will be strongly informed by this public consultation process and if any deficiencies in the rectifications suggested are uncovered by it, will suggest these are taken up with the local standard setter concerned prior to the equivalence process being taken any further. Finally, the length of any such consultation period would depend on any deadline imposed by the Commission on CESR providing its advice.

### ***EC determination of equivalence – Definition of equivalence***

32. An "overall" assessment of equivalence should be made in the final instance by the European Commission via a comitology process once all other steps have been fulfilled. According to Article 35.5E of the Commission Regulation 809/2004 on prospectuses and Article 2.5 of the Commission Decision 2006/891/EC of 4 December 2006:

*“At least six months before 1 January 2009, the Commission shall ensure a determination of the equivalence of the Generally Accepted Accounting Principles of third countries, pursuant to a definition of equivalence and an equivalence mechanism that it will have established before 1 January 2008 in accordance with the procedure referred to in Article 24 of Directive 2003/71/EC. When complying with this paragraph, the Commission shall first consult the Committee of European Securities Regulators on the appropriateness of the definition of equivalence, the equivalence mechanism and the determination of the equivalence that is made.”*

33. CESR has already provided the Commission with the definition of equivalence that it thinks should be used when making the determinations of equivalence (paragraphs 25-30 of CESR's advice 07-138). CESR defined that, for equivalency purposes, investors should be able to make a similar decision irrespective of whether they are provided with financial statements based on IFRS or on third country GAAP.
34. CESR's definition implies that the two equivalent sets of accounts lead to a similar investment decision at the time when that assessment is made. Therefore, any necessary remedies identified as part of the equivalence process should be applied in any set of accounts actually produced by a third country issuer using the GAAP deemed equivalent, except of course in cases where the necessary rectification is clearly not applicable to the issuer.

### ***Alternative approach for GAAPs with a programme of convergence to IFRS***

35. *CESR consulted on two different models for determining equivalence in its 07-212 consultation paper (appendixes 1 and 2). The second alternative model envisaged that in those cases where a convergence or adoption programme is in place and is being followed by the local standard setter, a short cut methodology might be put in place such that a GAAP could be considered equivalent as long as the stated convergence programme is being followed and its deadlines being sufficiently met. In such cases no additional disclosures would be required from issuers as long as these conditions are being fulfilled.*



36. Respondents to the consultation were split on this issue. Some respondents supported CESR's preferred model one, arguing that the fact that third country GAAPs may converge with IFRS at some stage in the future is of no relevance to a determination of whether the third country GAAP is currently equivalent to IFRS for the purposes of an investment decision being taken now.
37. On the other hand, some respondents stated that convergence programmes should be considered positively in decisions on equivalence. Such respondents observed that many third countries are making concerted efforts to converge with, or adopt, IFRS and that issuers from such countries would continue to use their local GAAPs up until 2009. If the transitional provisions were not in some way to be extended and these GAAP had not sufficiently converged with IFRS by the expiry of the transitional period in 2009, the outcome would be that such issuers would no longer be permitted to use their local GAAP. Respondents believed that the resultant change in reporting principles would likely confuse and disrupt the market and be an unwarranted burden on issuers.
38. Having fully analysed all the arguments put forward, CESR still considers that in the long term the appropriate way to assess the equivalence of third country GAAP with IFRS on the basis of CESR's definition of equivalence is through the mechanism discussed in this advice and summarised in appendix one of the paper.
39. However, CESR concurs that an extension of the transitional arrangements for those GAAPs currently converging to IFRS could avoid disruption of the markets and would allow those countries to complete their convergence with IFRS. Also, CESR would expect in any event that larger companies from such countries would see the benefit of adopting IFRS at an early stage, and would do so thus promoting its more widespread use. CESR believes however that such arguments are ultimately for EU legislators to assess.
40. For the abovementioned reasons CESR would advise the Commission to consider extending the transitional period for those GAAPs where a convergence programme is in place, is satisfactory in terms of addressing all significant differences to IFRS within an appropriate timetable and is currently progressing satisfactorily in accordance with this timetable. Should the Commission adopt such transitional measures, CESR would recommend not extending them beyond 2012. Finally, any new transitional measures should be granted only to those GAAPs currently accepted during the existing transitional period on account of their fulfilling the conditions set out in the revised article 35.5A paragraphs b) and c) of the Prospectus Regulation (and the similar provision in the Transparency Decision). This alternative is outlined in appendix two of this paper.

#### ***Filters at country and issuer levels***

41. CESR considers that a pre-requisite for any GAAP to be recognised as equivalent is that "filters" at the country level, and audit assurance and enforcement at the entity level are sufficient for investors to be able to rely on them. For the purposes of establishing equivalence, CESR assumes that third country GAAPs are properly applied including the provision of any rectifying disclosures necessary. CESR further assumes that the necessary filters for ensuring market confidence are in place for third country issuers using or participating in the EU capital markets.
42. CESR understands recital 8 of Commission Regulation 1787/2006 and recital 7 of the Commission Decision 2006/891/EC of 4 December 2006 as confirming CESR's view, highlighting the need not only of a technical parity between the standards, but also that the standards are adequately implemented:

*“The future assessment of equivalence should be based on a detailed technical and objective analysis of the differences between IFRS and third country accounting standards, as well as on the concrete implementation of these GAAP compared to IFRS.”*

43. One of the key filters set out by CESR in its June 2005 advice 05-230b relates to the audit of the financial statements concerned. Under the framework of articles 45 and 46 of Directive 2006/43/EC of the European Parliament and of the Council on statutory audit of annual accounts and consolidated accounts (“the 8th Directive”), the Commission, in co-operation with the Member States, is assessing the equivalence of third country legislation with the 8th Directive in relation to two areas: the first area relates to auditing standards and requirements on the independence and objectivity of auditors; the second area refers to the systems of auditor’s public oversight, quality assurance and investigations and penalties. In the absence of comitology measures granting equivalent status, a third country auditor who audits a third country company with securities admitted to trading on a regulated market will be required to register in a Member State and will be subject to its requirements. As far as CESR is aware such requirements would exist and apply to a third country issuer and its auditor whether such an issuer uses its own local GAAP, another equivalent third country GAAP or IFRS.
44. Consequently CESR believes compliance with the 8<sup>th</sup> Directive should be a relatively easy thing to establish about any jurisdiction that is applying for its GAAP to be recognised as equivalent. As the assessment also covers the main areas of control over possibly the key filter over the production of financial information it also serves as a reasonably objective proxy for any other specific assessment of the filters. CESR believes a step along these lines needs to be factored into the determination of equivalence of third country GAAP with IFRS because a key consideration for investors deciding parity between financial statements will be their overall reliability, and key to that decision is the robustness of the audit conducted on them.
45. For the avoidance of doubt CESR wishes to clarify that even if the legislation of a third country is not considered equivalent to the 8<sup>th</sup> Directive, the GAAP of such country can still be deemed equivalent if all the other steps in the mechanism are fulfilled. However, for an issuer from that country to be able to file in the EU financial statements (under its own local GAAP or IFRS), its auditor will have to be registered in a Member State and comply with the requirements of that State. This would also be considered to satisfy this assessment of filters step in the equivalence mechanism.
46. CESR would further take the opportunity to clarify that the assessment of the audit filter as proposed in the mechanism is dealt with exclusively through the assessment of compliance with the 8<sup>th</sup> Directive, including any transitional measures that the European Commission might introduce. Therefore, any transitional measures applied under the 8<sup>th</sup> Directive to the jurisdiction seeking equivalent status of its GAAP would be taken into account in the mechanism for determining equivalence of that GAAP.

#### *Other filters*

47. CESR also acknowledges that other filters, such as the corporate governance regime applicable to a third country issuer, will play a role in an investor's decision making process. However such areas are often highly issuer or business specific and as such are more difficult to assess objectively. CESR also considers that it is not unreasonable for an investor to make his own mind up about such factors based on his own risk appetite as, in the absence of Community legislation in this area relevant to EU issuers, he would have to do for an equivalent EU issuer.
48. *CESR invited interested parties to comment whether they considered that filters are important and whether they should be reflected in the equivalence mechanism. Again differing views arose from the consultation. Some respondents considered that the regulatory environment and other filters are not relevant in assessing whether a third country GAAP is equivalent to IFRS. Others stressed the difficulty of assessing filters objectively. However, in relation to the audit of the financial statements, a broad cross section of respondents supported CESR view that audit quality should be factored into the equivalence mechanism.*



49. *CESR still holds the view reflected in the paragraphs above and has not therefore changed its proposals published in the consultation paper.*

#### ***Auditor assurance regarding the remedies***

50. Any additional rectification procedures deemed necessary to render a GAAP equivalent to IFRS would be known at the time an audit on the year end accounts of any third country issuer using the GAAP is to be performed. Therefore the necessary work can be planned into the audit process to enable these additional disclosures to be audited. It should therefore go without saying that any rectification procedures suggested in Steps 1 or 2 of the mechanism (see the annexed chart) should be included within the scope of the audit of any set of accounts actually produced by a third country issuer using a third country GAAP that has been deemed equivalent.
51. CESR acknowledges that there may be technical difficulties with the concept of auditing disclosures that might be considered "outside of GAAP" but does not accept that this is a hindrance necessarily to this requirement being part of the equivalence process. CESR would therefore recommend that discussions are held with the appropriate third country applicant body during the assessment process to ensure that the rectification disclosures being suggested have sufficient status to ensure that an audit requirement in appropriate terms can be met in practice.

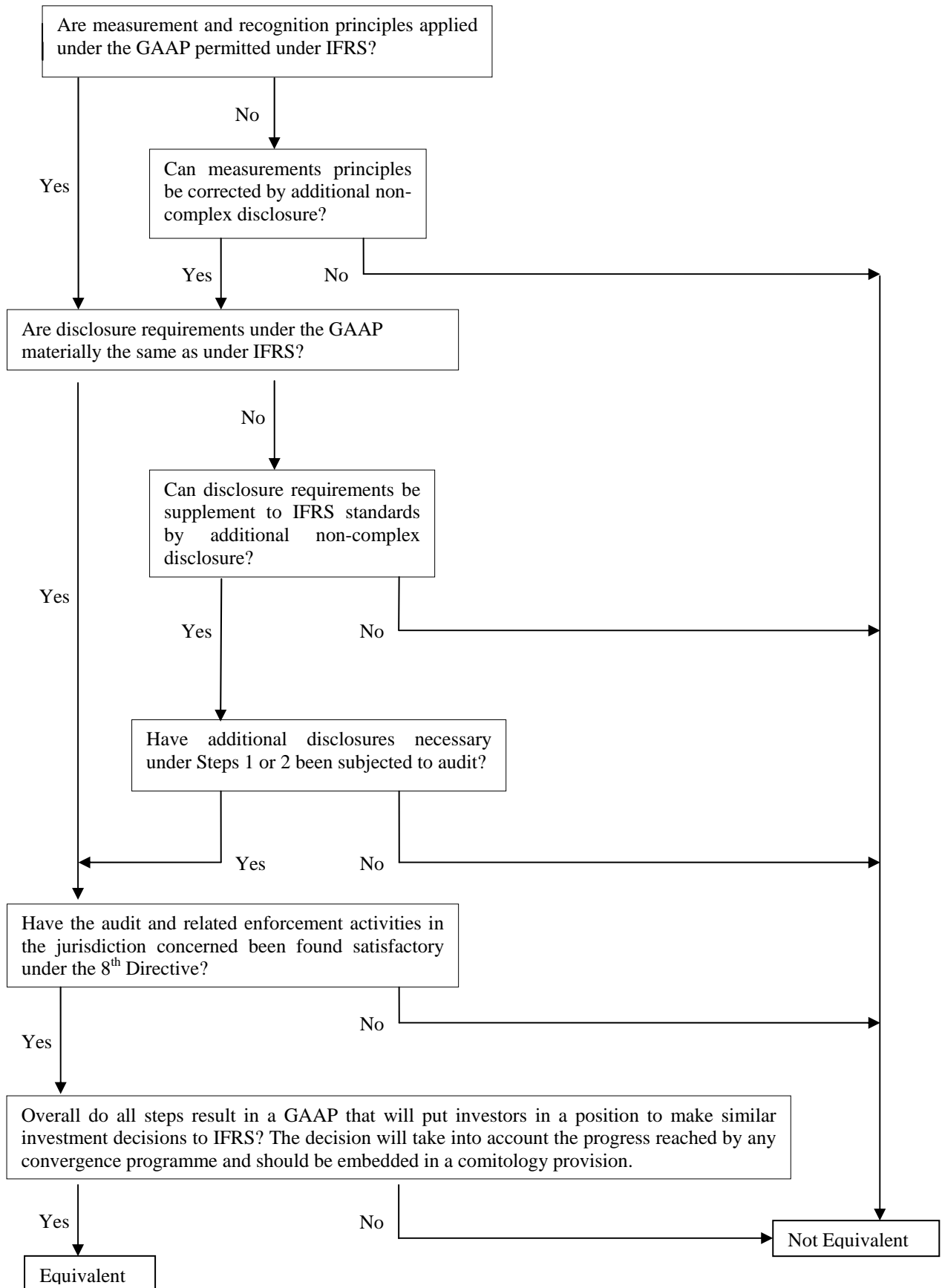
#### ***On going information from the standard setter***

52. Each time the local standard setter of an equivalent GAAP or the IASB issues a new standard, the local standard setter will need to submit to the European Commission (with a copy to CESR) an impact assessment of that new standard unless it has been issued jointly with the IASB. Any positive determination of equivalence by the Commission should be conditional on the local standard setter concerned agreeing to provide this information and update any rectification disclosures as appropriate for the effects of the new standard. CESR assumes that any new standards would include suitable transitional periods before their requirements take effect to allow issuers time to accommodate any necessary rectification disclosures in their accounts.
53. *Overall, market participants agreed with CESR's proposal. Some respondents suggested including a materiality test in the requirement to produce impact assessments. CESR considers that the concept of materiality is fundamentally embedded in the whole mechanism to determine equivalence contained in this advice, therefore, it should be apparent that only new standards that could lead to a significant difference between the equivalent GAAP and IFRS should be subject to the requirement advised in the previous paragraph..*

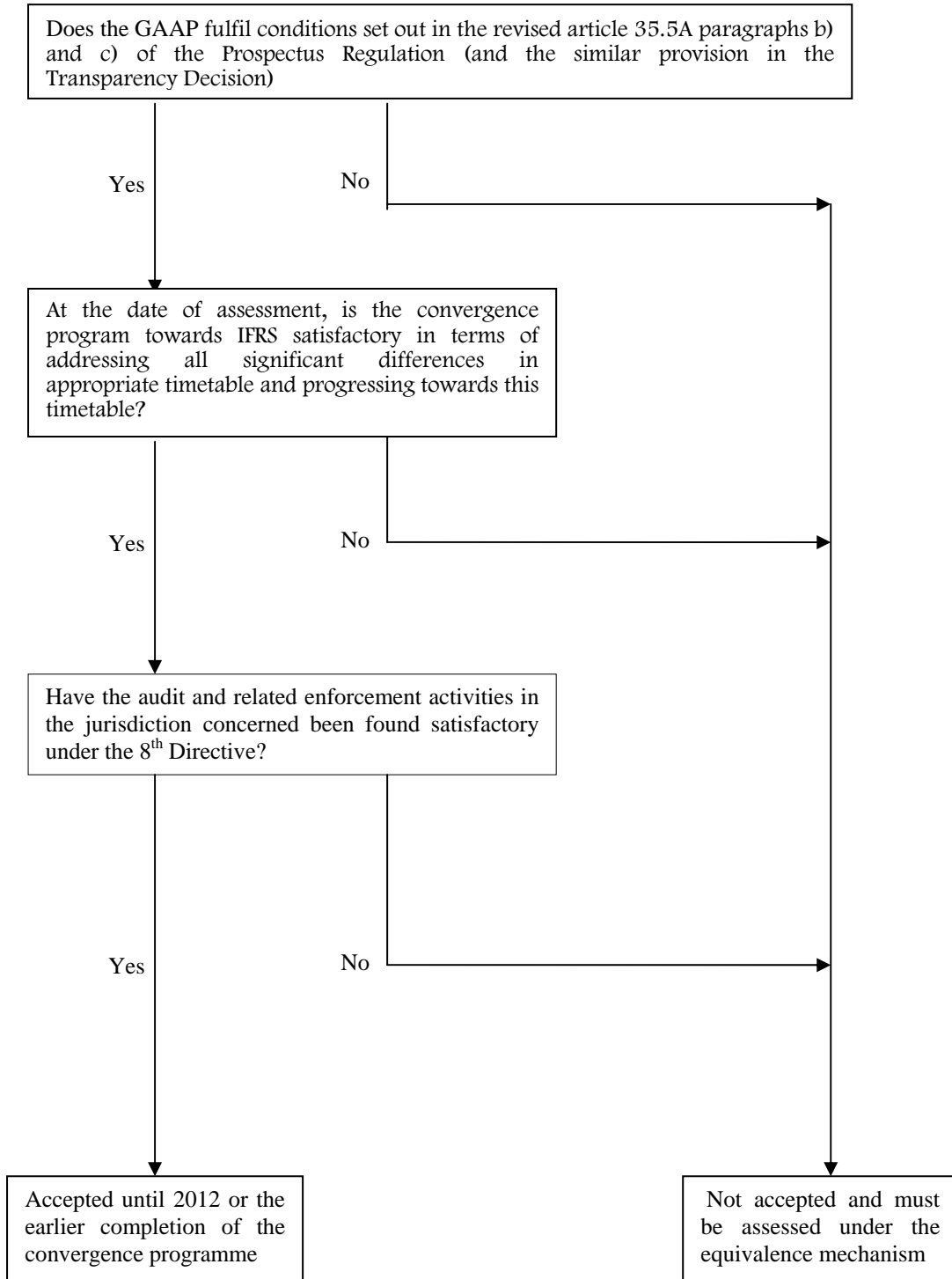
#### ***Enforcement in the EU of equivalent GAAP***

54. The GAAP equivalence process does not pre-empt enforcement activity in relation to issuers who use the equivalent GAAP. According to article 24.4 (h) of Directive 2004/109/EC of the European Parliament and the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market ("the Transparency Directive"), EU enforcers must have the powers to examine the financial statements to ensure they are drawn up in accordance with the relevant reporting framework and to take appropriate measures in case of discovered infringements.

**Appendix 1 - Mechanism for determining the equivalence of third country GAAP**



**Appendix 2 – Possible transitional measures for GAAP with a convergence programme to IFRS**





### Appendix III - Request from the European Commission to CESR for technical advice



#### EUROPEAN COMMISSION

Internal Market and Services DG

FREE MOVEMENT OF CAPITAL, COMPANY LAW AND CORPORATE GOVERNANCE  
Director

Brussels,  
MARKT/F3 JH/

Mr. Arthur Docters van Leeuwen  
Chairman  
Committee of European Securities  
Regulators  
11-13 Avenue de Friedland – 75008  
PARIS FRANCE

**Subject: Request for advice on equivalence under the Transparency Directive and Prospectus Regulation**

Dear Mr. Docters van Leeuwen,

I write to request the assistance of CESR concerning the equivalence of third country GAAPs under the Transparency Directive and Prospectus Regulation, and more specifically, creating the equivalence mechanism as envisaged by these legal measures.

According to the revised Prospectus Regulation<sup>7</sup> and the Decision regarding the Transparency Directive<sup>8</sup>, the Commission must establish a definition of equivalence, setup an equivalence mechanism and then determine the equivalence of third country GAAPs to a specified timetable. The legal measures require the Commission to consult CESR on each of these issues.

In order to start the process of determining equivalence, we are asking CESR for advice in four phases. This first letter contains the request regarding the first two phases.

In the first phase, we are seeking advice on issues needed for the first report to the European Parliament, and for the definition of equivalence. To this end, we are requesting a list of the GAAPs currently being used on EU markets as well as updates on the IFRS convergence in US, Japan and Canada. Details of this request for first advice can be found in the Annex 1.

In order to meet the deadlines specified in the Prospectus Regulation and Transparency Decision, we would be grateful to receive your first advice by the 1<sup>st</sup> March 2007.

---

<sup>7</sup> Revised by the Commission Regulation No 1787/2006 of 4. December 2006, OJ L337/17 from 5.12.2006 (see Annex 3).

<sup>8</sup> Commission Decision No 2006/891/EC of 4. December 2006, OJ L343/96 from 8.12.2006 (see Annex 4).



The second phase relates to the establishment of the equivalence mechanism. In the request for the second advice, the Commission asks CESR to advise in particular on how the equivalence of third country GAAPs should be assessed. Further details on this request can be found in Annex 2.

The requests for the third and fourth advice will be sent later on this year (the third request for advice with the advice of CESR to be received by 1<sup>st</sup> November 2007 and the fourth request for advice with the response to be received by 1<sup>st</sup> February 2008).

Yours sincerely,

Pierre DELSAUX

Contact: A. Leppilähti, +32 229 67961, R. Croci +32 229 92174, J. Hrudová, +32 229 53757

CC: J. Holmquist

Annexes:

- Annex 1: Request for first advice
- Annex 2: Request for second advice
- Annex 3: Commission Regulation (EC) No 1787/2006 of 4 December 2006 amending Commission Regulation (EC) 809/2004 implementing Directive 2003/71/EC of the European Parliament and of the Council as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements (OJ L337/17 from 5.12.2006)
- Annex 4: Commission Decision of 4 December 2006 on the use by third country issuers of securities of information prepared under internationally accepted accounting standards (OJ L343/96 from 8.12.2006)



## Annex 1: Request for first advice

### Request for first advice

#### **Description of the work programmes of the Canadian, Japanese and US standard setters, definition of equivalence and list of GAAPs currently used on the EU capital markets**

In order for the Commission Services to present a report to the European Securities Committee (ESC) and the European Parliament (EP) by 1 April 2007 and to satisfy their obligations to monitor and inform the ESC and EP about the amount of progress in convergence, we request the following advice from CESR.

Provide a description of the work timetable of the Canadian, Japanese and US standard setters, on the convergence between IFRS and the GAAPs of these countries (TD Article 2(1), PR Article 35(5B)).

Provide a description of the progress, to the extent possible, on these work programmes using the work that CESR carried out for its June 2005 advice to the Commission as a basis (TD Article 2(2), PR Article 35(5B)). NB: To the extent possible, the Commission would welcome assessment of the progress in convergence at this stage and asks CESR to bear in mind that a thorough report on progress in such convergence and on progress on the elimination of reconciliation requirements will be requested from CESR at a later stage to meet its obligation to "closely monitor and regularly inform ESC and EP about the amount of progress in this convergence and of progress on the elimination of reconciliation requirements" – TD Article 2(2), PR Article 35(5B)).

The Commission Services must adopt a legal measure, using comitology, on the definition of equivalence and the determination of equivalence by 31 December 2007 (TD Article 2(5), PR Article 35(5E)). To do this, a first draft of a legal measure will need to be presented to the ESC and the EP by June 2007. Therefore we also request the following advice from CESR.

Confirm the definition of equivalence (see below for details).

Provide a list of the GAAPs currently used on the EU capital markets (see below for details).

### Definition of equivalence

In order to establish the mechanism for determining the equivalence of third country GAAPs, we first need define equivalence for this purpose. CESR is therefore asked to advice on how the definition of equivalence should be formulated.





## GAAPs used on the EU capital markets

The purpose of this part of the request is to obtain as complete a picture as possible on the third country GAAPs that are currently used by issuers on the EU regulated markets. Over time, new issuers may use other GAAPs, but this list is an essential starting point.

CESR is asked to prepare, to the extent possible, a list of existing third country issuers that are traded on regulated markets in the EU specifying:

- their country of origin;
- the GAAP that they use; and
- whether that GAAP is reconciled to another GAAP; if so, what that GAAP is.

**Due:** CESR's initial advice is sought by the 1 March 2007.

## Annex 2: Request for second advice

### Request for second advice

#### Outline of the equivalence mechanism

The Commission Services must adopt a legal measure, using comitology, on the definition of equivalence and the determination of equivalence by 31 December 2007 (TD Article 2(5), PR Article 35(5E)). To do this, a first draft of a legal measure will need to be presented to the ESC and the EP by June 2007.

The Commission requests CESR to:

Advice on a suitable mechanism for determining the equivalence of a third country GAAP. This is not an assessment of which GAAPs are equivalent, but of the mechanism, or procedure, for making that assessment.

**Due:** CESR is asked to provide advice on these matters by 1<sup>st</sup> May 2007.

\* \* \*