



U.S. Securities and Exchange Commission

Speech by SEC Staff: International Developments: Convergence and You

by

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Thank you very much. I am delighted to have this opportunity to speak with you today about such a timely and critical topic. My goals today are to describe how international convergence is affecting U.S. standard setting and to encourage you to become an active participant in the process.

During the last 12 months, the accounting profession in the United States has been significantly challenged and changed. At the same time, momentum is building overseas towards creating a global financial reporting infrastructure, which would also be a tremendous change.

Perhaps the most significant of these international developments is the adoption of International Accounting Standards by at least fifteen different countries around the world. EU, Australian, and Russian public companies, among others, will be required to use International Accounting Standards in the next few years. For example, 7000 companies in the European Union will be required to adopt IAS by 2005. That's right - 7000 companies in the EU alone.

The anticipated conversion to international accounting standards by countries throughout the world has been the catalyst for a number of recent actions that are intended to encourage financial reporting consistency and transparency on a global level. These developments are not limited to the

convergence of accounting standards.

Currently, countries such as Canada, the UK, and Japan have efforts underway to introduce or improve minimum standards for audit quality assurance and to strengthen auditor independence. China had issued guidance related to professional ethics. And, the Committee of European Securities Regulators, or CESR, has issued for comment a Draft Statement of Principles on Enforcement.

All of these advancements are very encouraging and important to the continual development of the world capital markets. In the interest of investors, I assure you we will be closely monitoring all of these efforts.

The consequences of these and other international developments are already impacting preparers and auditors in the United States today, even though US GAAP continues to be our standard. Allow me to elaborate.

Convergence - What Does it Mean?

Convergence of accounting standards is the centerpiece of the efforts to build a global financial reporting infrastructure. And, the desire for convergence of accounting standards is greater than ever. Achieving this would greatly aid cross-border investing and decision-making.

While convergence can have a wide variety of different meanings, it is generally assumed that, ultimately, all standard setters should agree on a single, high-quality answer. The accounting standards setters at the IASB, in the U.S., and elsewhere are working together as never before. They are collaborating on projects and working toward convergence as they address urgent issues and improve accounting.

The SEC staff has encouraged both the FASB and IASB to develop reasonable and pragmatic short-term solutions to eliminating as many accounting principle differences as possible.

In particular, the US FASB and the IASB have recently published a memorandum of understanding regarding their plans for convergence of global accounting standards, a decision that was praised by many.

The recent memorandum of understanding is evidence that both Boards are working actively on solutions. In particular, the MOU specifies that both Boards plan to issue an Exposure Draft in 2003 related to convergence efforts.

Both Boards by virtue of the MOU have given high priority to work on "short-term convergence" - to iron out as many differences as possible with an eye towards the approaching conversion to IAS by specific countries. That priority is important, because improvements to the accounting model will go on forever.

With that said, by addressing numerous issues that can be resolved in the short-term, the Board should be able to reduce differences and make comparisons easier for investors.

Preparers and users of financial statements must be willing to accept that convergence of accounting standards will involve changes to both existing US GAAP and IAS. While it is premature to speculate about what changes may be forthcoming, it should be understood by everyone that achieving high quality accounting standards in a relatively short-time frame may involve picking the best of two accounting alternatives or developing an alternative approach that does not currently exist.

Changes in both US GAAP and IAS will occur, and it may be to the other way of thinking. Some may be initially uncomfortable with that. As examples, look at the effects of international efforts on matters in the U.S. on issues such as business combinations and financial instruments. And the FASB's revenue recognition project is part of a joint effort with the IASB.

And so even if you are a single line domestic manufacturing company with no foreign customers, your accounting may still change because of what's happening in London. At the end of the day, investors should be the winners because the convergence of accounting standards should provide more transparency and disclosure.

Both U.S. and international accounting standards have been criticized over the past few years. IAS has been criticized for being incomplete, too full of optionality, and lacking sufficient details to ensure comparable, consistent, and appropriate implementation.

In contrast, U.S. standards have been criticized for being overly detailed and complex and containing on/off switch rules that worship the form and not the substance of the transactions. And both sets of standards have been criticized for their use and proposed use of fair value measurements without providing the necessary implementation guidance and when the relevance of fair value as a measurement basis has been questioned.

What is needed is balance. Balance between the mixture of principles and rules. Balance in the level of detail of implementation guidance. And balance between relevance and reliability. Standard setters around the world have plenty of work ahead.

How Can Converged Standards be Effective?

Now, let me address the issue of whether converged standards can be effectively applied on a worldwide basis. Achieving consistent, comparable, and appropriate application of accounting standards may be difficult under IAS because of diversity of backgrounds and regulatory structures.

IAS will soon be applied in at least fifteen different countries in Europe and in

other regions of the world. We recognize that achieving the right balance of sufficiently detailed principles and base implementation guidance is extremely important.

Appropriate use of national and international interpretative bodies, such as the Emerging Issues Task Force in the U.S. and the International Financial Reporting Interpretations Committee, or IFRIC, is a critical element to the success of this effort. While not every question can be answered, there cannot be fifteen answers to a pervasive question as well. That would undermine the credibility of the system.

Let's talk about how to achieve proper and consistent application. Preparers and auditors should develop worldwide networks for communication and consultation on challenging questions.

Consultations should ensure that a consistent, high quality accounting or auditing solution is achieved. The use of cross-border experts should be formalized, and the principles being applied and any relevant precedents should be carefully considered.

Through this process, the difficult questions can be sifted out. By working together, everyone's interests, especially those of the investors we serve, can be advanced.

How Does This Impact Me?

At the beginning of my talk, I set out to describe how convergence is impacting you today. Just in case I have not been effective, let me talk specifics for a few moments.

- Did you realize that the FASB will soon begin deliberations on converging specific areas of US GAAP and IAS, with an Exposure Draft anticipated to be issued by mid-2003?
- Did you realize that the EITF has been encouraged by the FASB to coordinate activities with the IFRIC - and vice versa for the IFRIC and the IASB?
- Did you realize that the EITF is in the process of changing its operating procedures, and that they likely will more closely align with IFRIC?
- Did you realize that the FASB has a research project designed to identify, update, and monitor differences between US GAAP and IAS, with the goal to provide input to the FASB's agenda?
- Did you realize that the FASB and the IASB have split the responsibilities for the initial research and debates over short-term convergence issues, with the FASB focusing on matters such as research and development, nonmonetary asset exchanges, and others, and the IASB considering topics such as income taxes, discontinued

operations, and others?

What Else Can Accountants Do?

It is an exciting time to be an accountant. Global accounting standards are advancing rapidly. In light of those changes, let me leave you with a few additional thoughts for consideration.

Technical and other professional training programs take on a renewed importance in our current environment. Internal processes related to the conduct of audits could be bolstered by a focus on audit quality. Regulators will need increased cross-border communication regarding application of accounting standards.

The recent spotlight on the accounting profession will hopefully raise the bar in terms of education, training, execution, and overall quality control considerations for accountants and auditors everywhere.

Accountants and auditors can take advantage of events in the global marketplace to strengthen their competencies and refresh their companies' and firms' internal practices. I challenge you to just do it!

Conclusion

I leave you today with a few questions to ask yourself when assessing your accounting department or firm:

- Are international developments being monitored to determine the impact on domestic accounting work?
- Are education and training programs related to international accounting standards being rolled out to broaden technical competencies?
- Has a robust internal consultative process been developed that facilitates consistent, high quality solutions to accounting and auditing issues - both domestic and international?
- Are appropriate quality control procedures in place to oversee international accounting and auditing work?
- What else is being done to contribute to building a global financial reporting infrastructure?

Thank you for the opportunity to address you during what I believe is a historic time. I will be happy to take any questions during the Q&A.

<http://www.sec.gov/news/speech/spch121302jmd.htm>

