CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

July 28, 2011

Mr. James Kroeker
Chief Accountant
Office of the Chief Accountant
United States Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: SEC Staff Paper (May 26, 2011) on the Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers: Exploring a Possible Method of Incorporation

Dear Mr. Kroeker:

The U.S. Chamber of Commerce (the "Chamber") is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy.

To achieve these goals, the CCMC has been a strong advocate for a single set of global accounting standards and has supported efforts to improve standards and reduce complexity through the convergence of U.S. Generally Accepted Accounting Principles ("U.S. GAAP") and International Financial Reporting Standards ("IFRS"). The CCMC is submitting this comment letter and has also joined as a signatory to the Financial Instruments Reporting Convergence Alliance ("FIRCA") comment letter. The CCMC appreciates the deliberative approach of the Securities and Exchange Commission ("SEC") to determining whether, when, and how the current financial reporting system for U.S. issuers should be transitioned to a system incorporating IFRS.

The CCMC's comments are centered upon the following areas:

I. **Exploration of issues raised during the July 7, 2011 roundtable, primarily transition costs for mid-size and small issuers;**

II. **Completion of the convergence projects;**

III. **Alignment of non-converged U.S. GAAP and IFRS standards;**

IV. **Resolution of governance and due process issues;**

V. **Recognition of potential areas of permanent divergence;**

VI. **Need to address auditing issues; and**

VII. **Need for cost-benefit analysis.**

The CCMC believes that these issues should be fully vetted for the SEC to make the decisions necessary to determine the course of financial reporting in the United States.

These issues are discussed in further detail below.

Discussion

Overview

The world is a very different place than it was several decades ago when the goal of a single set of high quality global accounting standards was conceived and harmonization efforts got underway. Economic and geopolitical conditions have changed. In addition, it is important for the SEC to be mindful, before committing to making costly changes in the U.S. financial reporting system that companies of all sizes are currently attempting to navigate the challenges of a difficult economic recovery and implement a plethora of new regulations.

All things considered, CCMC suggests that it is time to acknowledge these conditions and that the SEC approach the issue of determining whether, when, and how the current financial reporting system for U.S. issuers should be transitioned to a system incorporating IFRS by first asking what is realistically achievable in today's environment that best serves the needs of all stakeholders— those in both U.S. global companies and U.S. domestic issuers.

In addressing this question, in addition to considering issues related to investor protection, business practices, and regulation in the current environment, the statement by Don Nicolaisen, then SEC Chief Accountant, in his Northwestern University *Journal of International Law and Business* (April 2005) article, "A Securities Regulator Looks at Convergence," seems to provide an overarching touchstone:

> *When I speak of IFRSs/U.S. GAAP convergence, I do not expect the two sets of standards will necessarily produce totally identical financial statements. But I do consider it necessary that convergence result in close alignment of the accounting for the same or essentially the same transactions, generally comparable results in trends and a continued cooperative will to reduce differences over time, as well as the transparent understanding of any significant differences.*

Additionally, it should also be kept in mind, by the SEC, IASB, and FASB, that the market capitalization of American public companies is the largest of any potential nation that could follow IFRS. Accordingly, the depth and size of American capital markets reflects special needs and issues that must be addressed for the United States to move forward and for IFRS to become a true global standard. At this point in time it is unclear if the IASB is willing or able to address these special needs.

I. <u>July 7, 2011 SEC Roundtable on IFRS—</u> Transition Costs for Mid-Size and Small Issuers

The CCMC commends the SEC Staff for its extensive efforts to develop and execute the Work Plan to consider the many factors relevant to a Commission determination on IFRS. In addition to the Staff Paper of May 26, 2011 ("Staff Paper"), these efforts have included the IFRS Roundtable on July 7, 2011 ("Roundtable").

The Roundtable provided a very open and useful dialogue with perspectives on a number of issues relevant to any transition of the financial reporting system for U.S. issuers to IFRS, including the costs and benefits of any such transition. In this regard, the Roundtable highlighted concerns about the costs of a transition, especially for mid-size and smaller issuers— many of whom anticipate no individual benefit, per se, in having to move their reporting to IFRS. Thus, the CCMC supports one of the principles of the Staff Paper – namely to focus on minimizing transition costs, particularly for smaller issuers.

The SEC's experience with the implementation of Sarbanes-Oxley ("SOX") Section 404(b) for non-accelerated filers should be a cautionary tale for the need to identify these costs and address those issues thoughtfully. A failure to do so could result in a backlash with domestic and international ramifications.

One potential solution is the creation of an Issuer Advisory Group ("IAG") made up of large cap, mid cap and small cap public companies.[1] The IAG can act as a means for the SEC to identify financial reporting issues and develop solutions. By using different strata of market capitalization, the SEC can have the flexibility to address the needs of issuers and investors alike.

The Roundtable also helped to illuminate the depth and breadth to which U.S. GAAP is embedded in the contractual and regulatory infrastructure in the U.S. Thus, the CCMC agrees with the basis of the Staff Paper—retaining U.S. GAAP and having the Financial Accounting Standards Board ("FASB") follow some type of endorsement process to substantially align U.S. GAAP with IFRS and maintain that alignment going forward.

The Staff Paper outlines one approach to such an endorsement process. However, so much continues to be in flux related to the standard-setting activities of the FASB and IASB, as well as with IASB governance, it is difficult to make a definitive assessment of the process described in the Staff Paper. Nonetheless, the CCMC has concerns about the predicates for an SEC decision on IFRS incorporation

[1] See February 1, 2011 CCMC letter to FASB and IASB on *FASB File Reference: No. 1890-100, FASB Discussion Paper and IASB Request for Views on Effective Dates and Transition Methods* ("February 1, 2011 letter"), see also the March 25, 2011 letter from FIRCA. These letters outline a series of proposals to address implementation issues and reduce the complexity of the FASB-IASB convergence projects.

whether to incorporate IFRS in the U.S. financial reporting system and for specifying any FASB endorsement process that would ensue from that decision.

There has also been some discussion of optionality, allowing some larger companies to be given the option to use IFRS, as promulgated by the IASB. The rationale for such an approach is logical for those companies that access global capital markets and have extensive international business. Optionality for these companies would be in line with the SEC decision several years ago to allow IFRS filers to no longer reconcile financial statements to U.S. GAAP. While this approach may be favorable, it should also be investigated to determine if such a path would be beneficial for investors and not result in an adverse balkanization of American financial reporting systems.

II. Completion of the Convergence Projects

The convergence projects of the FASB and IASB are a critical step in the advancement towards substantially aligning U.S. GAAP and IFRS and thereby enabling investors, businesses, and other interested stakeholders to evaluate, compare, and use financial data through a common language. However, the convergence projects are not yet finished and many difficult issues remain to be resolved. At this stage, it is not a given that U.S. GAAP and IFRS will converge in the areas subject to the Memorandum of Understanding ("MoU").[2] Nonetheless, the Staff Paper assumes such convergence.

It is important to recognize that a lack of unified FASB and IASB standards on the convergence projects complicates transitioning U.S. reporting to IFRS. On the one hand, it would result in accepting substantial differences between U.S., GAAP, and IFRS from the outset. Moreover, it would raise questions about the viability of the FASB working with the IASB in the future to resolve their differences prior to the promulgation of IASB standards. As such, it would undermine another assumption in the Staff Paper that modifications in IFRS would be rare under any FASB endorsement process.

[2] The MoU projects consist of those on financial instruments, revenue recognition, leases, the presentation of other comprehensive income, fair value measurement, balance sheet netting of derivatives and other financial instruments, and the consolidation of investment companies.

On the other hand, a two-step process that implemented new U.S. GAAP on the convergence projects, followed by an implementation of different IFRS requirements would be unduly burdensome on all participants in financial reporting, including preparers, users, and regulators. The convergence projects are a "litmus test" for the viability of any future IFRS endorsement process by the FASB. It is essential that the FASB and IASB work together and take as much time as necessary to reach agreement on standards related to these projects that are substantially converged.

III. Alignment of Non-Converged U.S. GAAP-IFRS Standards

The convergence projects are just the "tip of the iceberg" for mitigating substantial differences in the content of existing U.S. GAAP and IFRS. The Staff Paper classifies the convergence projects as Category 1 and the other standards in U.S. GAAP as either Category 2 (those encompassed by the IASB's ongoing and anticipated standard-setting activities) or Category 3 (all others). However, the Staff Paper lacks specificity on what Categories 2 and 3 contain, so it is difficult to assess any endorsement approach, including the approach outlined in the Staff Paper. In particular. Category 3 likely contains much of working infrastructure of U.S. GAAP, including industry-specific guidance, some of which has no corresponding guidance in IFRS.

Thus, the CCMC recommends that the SEC work with the FASB and IASB to catalogue U.S. GAAP in Categories 2 and 3, specify how U.S. guidance in each Category differs from IFRS (including where IFRS has no guidance), and identify areas in IFRS with no corresponding guidance in U.S. GAAP. Then, the SEC Work Plan should provide clarity around whether and how the FASB and IASB will address and resolve the differences.

One source of difference between U.S. GAAP and IFRS is interpretative guidance, of which IFRS has little. The reluctance of the IASB and its Interpretations Committee to provide such guidance was a topic of discussion at the SEC Roundtable, and concerns were expressed that the current IASB approach would be inadequate to meet the needs of stakeholders in the U.S. Nonetheless, the Staff Paper contemplates that the FASB would first work through the IASB for supplemental or interpretative guidance and that FASB "modifications [to IFRS] should be rare and generally avoidable"[3]. Further, the Staff Paper suggests that additional disclosure requirements might be one FASB response if an acceptable solution is not reached or the issue needing interpretative guidance is not being timely addressed by the IASB. However, disclosure is not the answer to overcoming problematic accounting or the limitations of IFRS for U.S. issuers.

Achieving a point in time whereby needed modifications to IFRS by the FASB are rare is even more questionable given the likelihood for unique financial reporting issues to emerge in the U.S. market. In the U.S., the FASB's Emerging Issues Task Force (EITF) plays an important role in anticipating, identifying, and facilitating the process to timely address emerging issues. In spite of its demonstrated effectiveness, the Staff Paper does not appear to contemplate the continuance of the EITF. The CCMC is concerned that the interaction process between the FASB and IASB (or the IASB Interpretations Committee) described in the Staff Paper is not likely to be adequate to consider and resolve emerging issues in a timely way.

IV. Resolution of Governance and Due Process Issues

Consistent with prior statements by the Commission, the Staff Paper retains the FASB as the U.S. standard-setter. However, the role of the FASB is contemplated to considerably differ from its current role. Essentially, the FASB "would participate in the process for developing IFRS, rather than serving as the principal body responsible for developing new accounting standards or modifying existing standards under U.S. GAAP"[4]. Also, according to the Staff Paper:

> *The FASB would play an instrumental role in global standard setting by providing input and support to the IASB in developing and promoting high-quality, globally accepted standards; by advancing the consideration of U.S. perspectives in those standards; and by incorporating those standards, by way of an endorsement process, into U.S. GAAP. Additionally, the FASB would become an educational resource for U.S. constituents to facilitate the understanding and proper application of IFRS and promote ongoing improvement in the quality of financial reporting in the United States.*[5]

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[3] See Staff Paper, page 10.
[4] Ibid, page 8.
[5] Ibid, page 8.

The Staff Paper goes on to list a number of ways that the FASB's participation in the IASB's standard-setting process could occur. In reviewing this list[6], the CCMC is concerned about the lack of formal mechanisms by which the FASB would have a voice in the activities of the IASB. Frankly, the list seems to relegate the FASB to becoming an extended staff of the IASB. The Staff Paper goes on to recognize the lack of formal mechanisms by stating that the FASB would "represent U.S. interests broadly in the standard-setting process, by participating in the standard-setting effort and sharing its views with the IASB both informally and likely also ***through written comment letters***" (emphasis added)[7].

The FASB needs to have an elevated role to assure it has a strong voice in global standard-setting. Formal mechanisms need to be in place within the IASB structure to ensure this occurs. The IFRS Constitution recognizes the importance of national standard-setters and provides for the IASB to have mechanisms for giving national standard-setters a voice. For example, the IFRS Constitution states: "The IASB will, in consultation with the Trustees, be expected to establish and maintain liaison with national standard-setters, other standard-setters, and other official bodies with an interest in accounting standard-setting in order to assist in the development of IFRSs and to promote the convergence of national accounting standards and IFRSs"[8]

Recent events reinforce the need for formal mechanisms to assure a strong voice for the FASB. For example, on June 24, 2011, the Trustees of the IFRS Foundation ("trustees") announced some modifications in the IFRS Advisory Council. The modifications include inviting regional standard-setting bodies to join the Council instead of national standard-setters. While the Trustees characterized this as a minor modification, it would result in the FASB not even having a seat at the Advisory Council table. Even though it is rather a large group, the IFRS Advisory Council is formally recognized by the IFRS Constitution as the body for giving advice to the IASB on agenda decisions and priorities in the IASB work; informing the IASB of the views of the organizations and individuals on the Advisory Council on major standard-setting projects; and giving other advice to the IASB or the Trustees. Thus, this modification appears to effectively silence any voice that the FASB would have as

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6 Ibid, page 9.
7 Ibid, page 13.
8 IFRS Constitution, Paragraph 28

a national standard-setter through currently established formal mechanisms of the IASB.

It is also important for stakeholders to have direct input into the standard setting process. Such a dialogue is helpful for an understanding of a project and to give standard setters' information and consideration of issues. Such a system of input requires a defined system of due process to insure fairness and appropriate parameters of discussion. While the CCMC has advocated for due process reforms on the part of FASB and the Public Company Accounting Oversight Board ("PCAOB"), there is currently a system in the United States to provide such input.[9] The CCMC is concerned with recent developments within the IASB to create regional forms of input and complaints at a recent Trustee's meeting where commenter's raising of due process concerns was disparaged.

FASB and the Financial Accounting Foundation ("FAF"), under the respective leadership of Chairman Leslie Seidman and Chairman Jack Brennan, have solicited feedback and input on an unprecedented scale by all stakeholders. While the CCMC's proposals have sought to institutionalize this approach, we have been extremely pleased with the outreach efforts of FASB and FAF and believe that this level of continuous dialogue has benefited the convergence process. Such systems must be recreated by IASB, with an avoidance of unnecessary layering which may prevent direct input. Additionally, the CCMC believes that the SEC should identify legal requirements, embedded in legislation, including, but not limited to the Securities Acts, SOX, and the Dodd-Frank Wall Street Reform and Consumer Protection Act that may need to be addressed regarding governance issues.

Although the Staff Paper does not focus on such matters as IASB governance, funding, due process, and accountability, all these would come into play as part of any Commission decision on IFRS for U.S issuers. For example, the Staff's overall Work Plan includes addressing the necessary issues to ensure that accounting standards are set by an independent standard-setter and for the benefit of investors. In this regard, the CCMC notes that substantial progress on important aspects of these matters is elusive particularly on ensuring stable, sustainable, independent funding of the IASB.

[9] See testimony of Thomas Quaadman before the U.S. Senate Subcommittee on Securities, Insurance and Investment, April 6, 2011 ("April 6, 2011 testimony").

Finally, the Staff Paper describes the role of the SEC if the United States adopts IFRS. The Staff Paper clarifies that the Commission would maintain its oversight over the FASB as the designed U.S. standard-setter, however, "the Commission would have a less direct oversight relationship with the IASB"[10]. The Staff Paper contemplates a framework where "the SEC would be actively engaged in the standard-setting process and with the broader activities of the IASB and its governance bodies"[11]. But, the Staff Paper does not discuss potential impediments to the SEC's active engagement with the IASB, including potential budgetary and other resource constraints.

Further, the SEC has a long-standing and well-honed working relationship with the FASB, which is not currently duplicated with the IASB or contemplated to be so. In addition, the SEC, FASB, and the Public Company Accounting Oversight Board ("PCAOB") regularly meet and work together to identify and address issues that arise in practice.[12] It would be helpful to better understand how the IASB would fit into these working relationships. There is also a need for a durable commitment by the IASB to accept the role of the SEC as a partner to warrant that accounting standards are in conformance with the necessary legal and policy standards.

The CCMC also believes that the SEC should undertake the recommendation of the SEC Advisory Committee on Improvements to Financial Reporting ("CIFiR") to create a Financial Reporting Forum ("FRF") made up of standard setters, regulators and stakeholders to identify short-term and long-term financial reporting issues and solutions.[13] This will help act as a safety valve to prevent problems in financial reporting and assist in the FASB-IASB governance process. The FRF will allow the SEC to have an active continuous role in financial reporting governance, even under an IFRS system.

V. <u>Recognition of Potential Areas of Permanent Divergence</u>

[10] Staff Paper, page 11.
[11] Ibid.
[12] Roundtable participants noted that the PCAOB can have significant influence on the interpretation of accounting standards through, for example, PCAOB inspection of registered public company audit firms.
[13] See April 6, 2011 testimony.

It should also be noted that the vast majority of nations that are using IFRS do not do so in a pure form and that nationalistic or regional differences exist. Because of the established pattern and practice of financial reporting and depth of the capital markets in the United States we believe that any adoption or use of IFRS will be no different.

In our past comment letters we have stressed the need to retain the Last in First Out ("LIFO") accounting method. LIFO has been an accepted accounting method under the Internal Revenue Code for over 70 years. Businesses that use LIFO assume for accounting purposes that they sell first the inventory most recently acquired or manufactured. Industries that often experience rising inventory costs typically account for inventory using the LIFO method. This is because LIFO accounting allows them to match current sales income with the current higher cost of that inventory. In short, the LIFO method enables businesses to avoid phantom profits caused by inflation. Repeal of LIFO accounting would result in a punitive, retroactive tax increase for businesses, placing significant cash constraints on them and limiting their ability to manage inflation. Companies would have to record illusory profits on their books, when no economic activity has occurred that would justify recording any profits. Accordingly, to avoid these negative ramifications, we strongly recommend that the existing LIFO accounting method remain in place.

The CCMC has also raised concerns with the stress of our litigation system upon IFRS. There has been a delicate balance in place regarding financial reporting concerns and legal rights in the recognition of loss contingencies. That need for balance has been underscored by the debate concerning potential changes to the FAS 5 standard, while the CCMC also strongly opposed the proposed IAS 37 standard by the IASB.[14] Accordingly, it is the opinion of the CCMC that IAS 37 is insufficient to withstand the crucible of the American litigation system.

VI. Need to Address Auditing Issues

Auditing is, obviously, a crucial factor in providing all stakeholders reliability in the use of financial statements. As such, the auditor and audit policies can have a

[14] See May 17, 2010 letter from the Chamber to IASB on the Exposure Draft ED/2010/1, *Measurement of Liabilities in IAS 37*. The Chamber in its letter requested that the proposed revision be withdrawn.

dramatic impact upon accounting standards. Indeed, the auditor can change the nature and scope of an accounting standard in real practice.

Because of these concerns, the CCMC has also held the strong view that there needs to be a convergence of auditing standards to create a global audit standard that accompanies global accounting standards. Indeed, the PCAOB is undertaking an aggressive rulemaking regime and the European Union is going down this path, in its own way.

A failure to insure that audit and accounting policies are on the same page would, in our opinion, be a disaster for a global accounting standard. Inconsistent auditing around the globe can undo all of the hard work undertaken by FASB and IASB. The CCMC recommends that the SEC insure that the PCAOB, FASB, and IASB are working together to provide for common standards and consistent interpretation. As stated earlier, the FRF will be integral to insure this appropriate level of discussion and coordination.

VII. Need for Cost-Benefit Analysis

As discussed earlier, the impacts of using IFRS can have radically different costs and benefits to different issuers or class of issuers. While costs and benefits are not outcome determinative, they are an important tool to determine the utility and application of rules.[15] The use of a cost-benefit analysis will help provide the SEC with crucial information needed to make the necessary decisions on IFRS, determine problems that may need to be addressed, as well as provide a more articuable basis of benefits for the economy. This information will also be helpful to issuers and investors in evaluating these issues.

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Again, the CCMC appreciates the SEC's thoughtful and deliberative approach to this important issue.

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[15] On July 7, 2011, President Barack Obama signed an Executive Order requesting independent agencies to follow Executive Order 13563 in the development of rules and regulations. Executive Order requires a more rigorous use of cost-benefit analysis and directs agencies to use the least burdensome in the development and application of a rule.

In conclusion, the CCMC appreciates the opportunity to comment on the Staff Paper. In closing, we would like to reiterate a point that has been previously stated in comment letters supporting efforts to improve standards and reduce complexity through the convergence of U.S. GAAP and IFRS. Quick-fixes to converge U.S. GAAP and IFRS do not serve the interests of investors and other financial statement users. Convergence for convergence sake is not an appropriate goal or outcome. The interests of all stakeholders are best served by the promulgation of accounting standards that will serve the test of time.

Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

Tom Quaadman