

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

28 July 2011

Re: 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" (Securities and Exchange Commission "Staff Paper") (File No. 4600)

Dear Ms. Murphy:

Ernst & Young LLP is pleased to provide feedback on the Securities and Exchange Commission Staff Paper regarding a possible method of incorporating International Financial Reporting Standards (IFRS) into the financial reporting system for US issuers.

We support the approach described in the Staff Paper. We believe it is a thoughtful and balanced way of moving closer to achieving the ultimate goal of a single set of high-quality globally accepted accounting standards.

Ideally, we would like to see a single set of high-quality accounting standards used throughout the world, including the US, without modification. However, we unfortunately are not convinced this worthy goal can be practically achieved at this time. Certain countries have adopted a "local flavor" of IFRS (although to date we note that the modifications often have not been significant) or appear headed in that direction. As the SEC staff has observed, in most jurisdictions full adoption of IFRS as issued by the IASB, without an endorsement process, is rare. Few nations are willing to sacrifice their accounting standard-setting sovereignty, particularly for issues they view as important to their local capital markets and economies. We doubt constituents in the US will be more willing to make this sacrifice. Therefore, some form of endorsement process seems necessary and the creation of a "US flavor of IFRS" inevitable.

However, we believe the framework described in the Staff Paper is a reasonable alternative that, while not ideal, could help address US political, regulatory and other concerns while at the same time moving us closer toward a reasonably converged set of global accounting standards.¹ In addition:

- ▶ We recognize that the SEC cannot and should not abdicate its responsibility over financial reporting for US issuers and support its continued oversight of US GAAP for public companies. Adopting this framework would result in closer alignment of US and international accounting and financial reporting standards while maintaining the ultimate standard-setting and regulatory authority for those standards in the US. However, as is the case today, the SEC would have to exercise its authority by providing its input during the standard-setting process, rather than unilaterally creating or revising GAAP for US issuers, for this approach to more successfully converge US GAAP and IFRS.
- ▶ We would support the continuing role of the Financial Accounting Standards Board (FASB) as the US national standard setter and would support its active participation in the International Accounting Standards Board's (IASB's) standard-setting process, which is broadly consistent with the role of other national standard setters. It would be particularly critical for the perspectives of US constituents to be heard and considered throughout the IASB's standard-setting processes. The FASB's role, as described in the Staff Paper, would be instrumental in providing that input and support to the IASB in developing and promoting high-quality, globally accepted standards. We agree that this would be a different role from that which the FASB currently plays, and we support this proposed approach because it aligns the FASB more with other national standard setters.
- ▶ We also would support a process in which the FASB would evaluate IFRS for incorporation into US GAAP by following a well-developed and pre-established endorsement and incorporation protocol, with a high threshold for modifying the international standards. That threshold should focus on the acceptability of the specified international standard in the US, not necessarily the preferences of the FASB. We hope such a protocol ultimately would result in few deviations from IFRS as issued by the IASB, but recognize that differences may be necessary in certain circumstances to protect US public interest and investors.

Although we support the approach described in the Staff Paper, we believe it is unlikely that method would allow US issuers (following a transition period) to assert compliance with IFRS as issued by the IASB.

We note that the possible incorporation approach includes an objective that US issuers would be able to assert compliance with both US GAAP and with IFRS as issued by the IASB at the end of the transition period. While a very worthy objective, we believe it is unlikely to be achieved under the framework described in the Staff Paper for the following reasons:

¹ In its May 2011 Report of the Trustees' Strategy Review, the IFRS Foundation stated a goal of global adoption of IFRS in its entirety, without modification, but similarly recognized that convergence may be a step on the road to full adoption.

- ▶ Certain existing differences between US GAAP and IFRS will be difficult to eliminate (e.g., LIFO inventory accounting, accounting for contingencies). Even if the FASB initially agreed to eliminate all significant differences under a transition incorporation protocol, some constituents likely will strongly oppose eliminating certain differences, and the FASB and SEC will be forced to seriously consider such opposition. In addition, there may be US political or regulatory pressures to maintain certain elements of current US GAAP for various reasons.
- ▶ The FASB and the IASB have reached different conclusions on certain Memorandum of Understanding (MoU) projects (e.g., consolidation, financial instruments and balance sheet offsetting) and on other FASB-only projects currently under review (e.g., investment properties). It is therefore possible that the FASB would not eliminate all differences for these accounting topics, even when evaluating the international standard under a transition protocol. The FASB's support for ongoing differences might be similar to the justification for maintaining the differences today, which often is influenced by the views of US investors and other constituents. We believe the FASB may find it difficult to justify incorporating an IFRS standard into US GAAP if it had recently deliberated an issue included in the standard and reached a conclusion different from that of the IASB.
- ▶ IFRS 1, *First-time Adoption of International Financial Reporting Standards* (IFRS 1), is the "bridge" accounting standard used when a reporting entity applies IFRS for the first time. Reporting entities are required to apply IFRS 1, which includes a general presumption of retrospective application of IFRS (with certain specified exceptions), to assert compliance with IFRS as issued by the IASB. Without requiring the application of IFRS 1, or without a significant amendment to IFRS 1, we question how US GAAP in the foreseeable future, as contemplated in the Staff Paper, could be substantially equivalent to IFRS as issued by the IASB.

For the reasons stated above, we believe it unlikely that every major difference between US GAAP and IFRS would be eliminated under the method described in the Staff Paper. As a result, that approach likely would result in the creation of a "local flavor" of IFRS for the US market. We believe it is important for participants in the US capital markets, as well as global capital markets, to understand this likely outcome before committing to the process. While complete convergence may not be achieved at the end of the transition period, we would hope investors would be able to understand any remaining substantive differences between US GAAP and IFRS and financial statements prepared in accordance with each. We also would hope remaining differences would not represent a major impediment to cross-border capital flows. Constituents should understand this benefit and conclude that it is sufficient to justify the long-term investment required under the approach described in the Staff Paper. After reflecting on the approach, we believe this benefit does justify the investment. Again, while not ideal, the approach outlines a practical way to get us much closer to a reasonably converged set of global accounting standards.

We do not support a method that would create frequent change over an extended period for US issuers.

Notwithstanding our overall support for the approach outlined in the Staff Paper, we are very concerned with an environment in which the FASB might continually make changes to US GAAP (including through incorporating IFRS into US GAAP) over an extended period. While we understand some change would be unavoidable during the transition period envisaged by the framework, frequent

changes over an extended period for US issuers would have the potential to significantly disrupt the financial reporting system in the US.

To help minimize the amount of disruption the financial reporting community – preparers, investors, other users, academics and auditors – would be required to absorb, we hope the FASB would make changes to its legacy standards only to converge with IFRS. That is, we would not expect the FASB to change its standards unless convergence was being achieved. Legacy standards that will not be converged should not be modified during this transition period, with the exception of any updated implementation guidance.

In addition, we would hope that the FASB would carefully consider what changes are necessary to its legacy standards to achieve substantial convergence. We would expect the FASB to be judicious in making those changes, focusing on major areas of difference between US GAAP and IFRS that are viewed to be of particular concern to investors and other US GAAP financial statement users. We can envision an environment in which some differences would continue beyond the transition period, and while such differences could be substantive, we would fully expect them to be more modest in number.

After the FASB decides what changes to legacy standards should be made, we also would encourage it to explore approaches to adoption that would ease the transition burden for US issuers. For example, requiring preparers to adopt new accounting standards each year during the transition period would be unduly burdensome. We fully expect that the FASB would be sensitive to this issue, as it faces a similar challenge with the MoU projects that are presently approaching completion.

After the transition period, we would expect changes to US GAAP to follow corresponding changes made to IFRS by the IASB and would expect new differences between US GAAP and IFRS to be “rare,” as described in the Staff Paper.

We reserve our judgment as to whether the method described in the Staff Paper should represent the endgame or whether, in the future, the environment may have changed to one in which US issuers would fully adopt IFRS.

We currently are not in a position to form a view as to whether the possible incorporation method described in the Staff Paper should represent the final stage in the consideration of the full adoption of IFRS by US issuers. It is possible that after the successful implementation of the framework, the environment may be more conducive to adoption of full IFRS, especially if the majority of the significant differences between US GAAP and IFRS have been eliminated. On the other hand, we accept that this may not be the case. We nonetheless believe that maintaining US GAAP with more limited differences from IFRS would be acceptable for the reasons mentioned above.

We would support voluntary adoption of IFRS as issued by the IASB by US issuers.

Although it is not addressed in the Staff Paper, we would support an option for US issuers to adopt IFRS as issued by the IASB. The SEC currently allows Foreign Private Issuers (FPIs), which are some of the largest and most complex companies in the world with diverse ownership, to file their financial statements in accordance with IFRS as issued by the IASB, without reconciliation. At present, there are approximately 160 FPIs that file financial statements using IFRS, and that number is set to increase when Canada adopts IFRS in 2011. The SEC has already concluded that IFRS is of sufficient

quality to provide information necessary for the protection of US investors. This acceptance of IFRS for FPIs has resulted in a “two-GAAP” system within the US since the SEC began accepting IFRS financial statements for FPIs four years ago. As a result, US investors must become familiar with IFRS to make investment decisions about these companies. Providing US issuers with the option given to their foreign counterparts is equitable, and would not appear to place an undue burden on investors (who are already becoming familiar with IFRS).

* * * * *

We look forward to continuing to discuss this important issue with the Commission and its staff. The decision on whether and how to incorporate IFRS into the US accounting and reporting framework is a critical one. We commend the Commission and its staff on the thoughtfulness displayed in the paper and for considering the desires and needs of different participants in the US capital markets as it moves forward with its decision-making process on this important matter.

Very truly yours,

Ernst & Young LLP