The path forward for international standards in the United States

Considering possible alternatives

Highlights

- The SEC has stated it plans to make a determination on the future use of international standards by US public companies in 2011.
- Full acceptance or complete rejection of a move to international standards in the US seems increasingly unlikely. A compromise solution will likely be necessary.
- Completion of the current convergence agenda, enhanced cooperation among key capital market securities regulators and a refocused international interpretations body will provide a more solid foundation for a single set of high-quality global accounting standards.

The international standards' debate continues.

- The Securities and Exchange Commission has stated it plans to determine this year whether, when, and possibly how international standards should be incorporated into the US financial reporting system.
- Those involved in the US financial reporting system seem divided on the best path forward. Our sense is that some of the support is waning for full near-term mandatory adoption of international standards in the US.
- A May 2011 SEC staff paper describes a slower approach of incorporating international standards into the US financial reporting system, with an objective of US standards being compliant with international standards in perhaps five to seven years.
- We believe in the vision of a single set of high-quality global accounting standards. Achieving that vision will require more consistent application of international standards across jurisdictions that adopt them. The potential SEC staff approach is a fair starting point – and one that can be built upon to make progress towards this ultimate objective.

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Many possible paths to a common objective

Different, but valid and strongly-held, views exist as to whether and how the US should change to international standards.

The SEC staff suggested a possible compromise to start a dialog on potential transition approaches.

High quality accounting standards

The vision is powerful. Few dispute its attainment will have value for investors. A single set of high-quality, transparent, and robust accounting standards, consistently applied by companies in capital markets around the world will enhance the efficient allocation of capital. Worthy companies will find it easier to access low-cost capital to grow. Investor returns will improve. These outcomes are what many envision from a move to a single set of high-quality global standards.

For more than ten years, the world's two most significant standard setters, the FASB and IASB - collectively the boards - have brought US and international standards substantially closer together.

Throughout the process, the boards have dealt with many thorny, long-standing issues. In some areas of the literature they agreed to remove differences, in other areas they did not. While at times the process has been difficult and time-consuming, it has improved both sets of standards. On balance, most would agree that the process of bringing the two sets of standards closer together has been worthwhile.

Approximately 60 countries plus those in the European Union have adopted international standards, in some form, for publicly listed companies. However, adoption of international standards in all major capital markets will not, in and of itself, achieve the vision. This is because the protection of investors and the efficient allocation of capital globally can only be achieved when the common set of high-quality global accounting standards is also applied with reasonable consistency. A number of major capital markets have not fully adopted international standards as issued by the IASB. And some believe that the consistency of application of international standards, among those countries that have adopted them, should be improved.

Multiple paths; valid perspectives

The alternatives for integrating international standards into the US reporting system are numerous. They range from doing nothing - leaving US accounting unchanged, to abandoning US accounting and adopting international standards all at once, to many possibilities in between. Each has advantages and disadvantages and supporters with strongly-held views.

Those advocating leaving US accounting alone assert that it is well established, meets the needs of financial statement users, and has allowed US companies to have the lowest cost of capital.

Those advocating changing to international standards cite the benefits of increased global comparability for investors, lower preparation costs (ultimately), and easier cross-border access to capital.

Others acknowledge the long-term benefits of international standards, but say that a more gradual implementation process is needed. They believe such an approach could address the lack of a political mandate for change in the US, spread the costs over a longer period, and pragmatically address the multitude of issues that will be encountered.

Possible SEC staff approach

The SEC staff has been exploring a way to gradually incorporate international standards into the US financial reporting system. Under this scenario, US accounting would continue to exist. The FASB would endorse for use in the US acceptable new international standards resulting from joint or IASB-only projects. The FASB would also evaluate other existing international standards during this time and consider how to conform US standards to them. The ultimate objective would be for US standards to be compliant with international standards in perhaps five to seven years.

Compromise, flexibility and a slower transition

We believe in the vision - a single set of high quality, transparent and robust global accounting standards.

We are convinced that only international standards can be the foundation for this vision.

The SEC staff's suggested direction is a fair starting point in making progress towards achieving this vision.

No perfect solution

We support the thorough way the SEC staff has gathered input, and we are confident thoughtful deliberations will occur among Commission members as they decide the path forward. But based on the political and business landscapes, if an all or nothing decision is to be made, we fear it will be nothing. The US would stay with its own accounting - and in the long run, that would be unfortunate. Though sufficient support for change does not currently exist, in our view, progress toward achieving the vision should not stop.

Standard setters and regulators

Today, achieving the vision remains a longer-term objective. Though standard setters have worked diligently, and great progress has been made, all major convergence projects are not yet complete.

We believe that the boards should continue working together to finish the current convergence projects. After completing those projects, the boards should continue collaborating to enhance the quality of financial reporting in areas where common needs for improvement exist.

We realize that many inside and outside the US tire of convergence. Nevertheless, the benefits for investors of eventually getting to high-quality global accounting standards are worth the price of continued collaboration for a period of time.

In addition to improved standards resulting from convergence and collaboration, a key to achieving the vision is establishing an effective foundation to enhance the consistency of application. This would assist investors in attaining maximum benefits from high-quality global standards.

The regulatory and standard setting mechanisms to facilitate improved consistency in application are, for the most part, not yet in place or do not yet operate at a sufficiently high level. Enhanced cooperation and coordination is needed among national regulators, the IASB and its interpretive body, auditors, and preparers to facilitate more consistent application of international standards.

Allowing an option to change to international standards

If using international standards were allowed, most US companies would need at least four years to put in place the systems and controls necessary to adopt them. Also, the expected timing for issuance of standards resulting from the major convergence projects will likely be late in 2012. Given this timing, the retrospective adoption provisions, and the effort required of companies to make needed system and control changes, most interested US companies wouldn't adopt the new convergence standards or international standards until 2015.

Significant progress can be achieved between now and 2015 in standard setting and regulatory cooperation. For example, completing convergence projects, further improving international standards consistent with the IASB's new agenda, putting a foundation in place to enhance the consistency of application, and resolving numerous US transition issues can be accomplished. We believe that the SEC should monitor progress between now and 2015. If sufficient progress continues, the SEC should target the beginning of 2015 to allow US companies to optionally adopt international standards.

In conclusion

The potential SEC staff approach of slowly incorporating international standards based on assessing the quality of new and existing international standards is a fair starting point. It establishes a continuing role for the FASB and maintains the SEC's oversight of accounting standards used by companies that participate in the US capital markets. In addition, by addressing the practical consequences of making fundamental changes to US financial reporting, we believe the SEC staff is moving the ball forward.

Although the vision is clear, the pathway is not. More consistency, compromise, and a slower transition plan will increase support among US companies to move to international standards. Continued dialog and increased cooperation are needed, but the worthiness of the goal demands that progress continue to be made.

Questions and answers

Q: How can increased regulator collaboration facilitate more consistent application of international standards?

A: Increased collaboration can be achieved through greater focus on consistent application, improved communication between regulators, and cooperation agreements. One example of a cooperation agreement relates to companies seeking cross-border capital in public markets. Major capital market securities regulators could agree that any company purporting to follow IFRS and seeking public capital in another market, but not following that market's accounting principles, would be required to file periodic financial statements with the securities market regulator in which capital is being raised, using standards issued by the IASB.

The financial statements of those companies would be subject to reviews by regulators in the countries where capital is raised. If instances of non conformity with standards issued by the IASB are identified, those matters would be resolved through discussions between the company, their home market securities regulator, and the securities regulator where the filing occurs. In this way, these cooperation agreements would enhance the sharing of information and help to reconcile views.

Consistent application of international standards also would be enhanced through regulatory reviews aimed at identifying unacceptable differences in the application of international standards. Agreements among capital market securities regulators to refer interpretation and application differences to a refocused interpretations committee would also assist in achieving a higher degree of reasonable consistency.

Q: Some suggest that companies should be permitted to move to international standards as early as possible. You suggest such an option should be targeted for the beginning of 2015. Why?

A: As a practical matter, key convergence standards are not expected to be effective until 2015 at the earliest. Even if early adoption of these new standards were allowed, because of the changes needed to systems and controls to implement them, and the retrospective adoption requirements, we believe many companies would not want to adopt them before 2015. Preparations to use international standards would take at least as long. As a result, we believe the SEC should use the time leading up to 2015 to monitor further development of international standards and the progress toward putting a foundation in place to improve the consistency of application. If sufficient progress is made, the SEC should allow US companies the option to change.

Q: The SEC staff paper envisions an endorsement process that allows the FASB to modify international standards as they are incorporated. Will this work against the goal of a single set of global standards?

A: The ability to modify standards through endorsement could result in a US "flavor" of international standards. This is why the threshold for making modifications is so important. Careful consideration must be given to the criteria. We believe that the threshold should be set at a level that would result in minimal modifications. The SEC staff's suggestion that the threshold consider "the public interest and the protection of investors" is a good starting point.

Contact Information

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