



## U.S. Securities and Exchange Commission

### **Speech by SEC Staff: Remarks Before 2006 AICPA National Conference on Current SEC and PCAOB Developments**

*by*

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#### **Introduction**

Good afternoon. I appreciate the opportunity to join you again today. Let me note that my first thought in preparing today's remarks was that the points in my speech from yesterday probably bear repeating, but alas I will not put you through that. Let me also say that I have not gained any more authority since yesterday, so the remarks I make today are also my own and do not necessarily reflect those of the Commission, the Commissioners or of other members of the Commission's staff.

#### **Today's Remarks**

From my vantage point as a securities regulator, I am able to observe several aspects of the development and use of the International Accounting Standards Board's International Financial Reporting Standards (IFRS). But as you are practitioners, I know that you and I have one vantage point in common; that is, a window into the application of IFRS in practice. This is the matter that I would like to cover today because, quite frankly, people have asked us to share whatever we can about the nature of the questions the SEC staff has so far raised in its comment letters to foreign registrants on the application of IFRS, or on jurisdictional adaptations of IFRS that have identical provisions. While the SEC staff comment letters that contain this information — and the company's responses as well — are available to the public on our web site not earlier than 45 days after the staff has completed a filing review, I nonetheless understand that people are looking for information as they approach year end. Let me also say that my remarks are not a travelogue of the various ins and outs of IFRS, so hopefully those of you who spend most of your time with US GAAP will get something out of

them as well.

The basis for my remarks is the nature of the questions raised by the SEC's Division of Corporation Finance in its first comment letters to fifty or so of the foreign registrants who filed 2005 "home country" financial statements prepared under either IFRS or jurisdictional adaptations of IFRS. Some of those registrants have replied. Reviews of the 2005 filings of other foreign registrants are also on tap. I thus can't overemphasize the in-process nature of this work. Accordingly, my remarks today are not in the form of any opinions or conclusions about any good, bad or indifferent aspects of IFRS or its application in practice; rather, my remarks consist of factual information about the nature of questions that to-date the SEC staff has asked and, as with my remarks yesterday, a "what I wonder, as I wander" element as well.

As a reminder, the concept of these SEC staff reviews of foreign registrant filings is not new. The Sarbanes-Oxley Act calls for such reviews at least once every three years. Home country financial statements continue to be in the scope of these reviews because they, too, are information that a foreign registrant presents for consideration by investors in the U.S. capital markets. The SEC staff's practices to consult on certain troublesome points of home country GAAP with the home country securities regulators also play a part. I certainly welcome that input, while others have told me that this gives them comfort also.

## **Nature of SEC Staff Questions**

Let me categorize my remarks into two areas: questions about presentation and questions about disclosure. First, to presentation.

### **Presentation**

First, with respect to overall layout, some questions relate to information that is called for by IFRS that seems to be located outside the financial statement portion of the filing, without any form of reference from the financial statements to it. An example of this is information about the terms of share capital. In these cases the financial statements themselves thus are missing this information; also omitted is the auditors' assurances thereon.

Second, while not a question area per se, the staff has noticed that sometimes information provided in the financial statements and footnotes tends to be a little "all over the place." Perhaps some of these layout matters stem from the IFRS financial statement template being legacy financial statements based upon previous accounting standards, plus the new stuff. If there is a minute to look at overall layout for 2006 financial statements, that might be beneficial to providing transparent and understandable information to investors.

Third, as presentation questions relate to individual financial statements, the SEC staff has asked questions around what is labeled "operating income" as well as the starting points for the calculation of operating cash flows. Now, let

me move to disclosure.

## Disclosure

Let me begin by stating that the basis for disclosure questions is what the company has — as in, does it own investment property or does it use derivatives — relative to the disclosures that IFRS calls for. Questions raised by the staff on disclosure have covered the full range of accounting topics. Thus, rather than topic-by-topic, a better way to look at the questions regarding disclosures is to think of the nature of the questions. For ease of communication I have grouped these into three categories; namely what I will call disclosure that appears to be omitted, disclosure that is difficult to understand and disclosure that appears to be shallow.

The first category of comments is about disclosures that simply appear to be missing. The name given to this category is rather self-explanatory. Information that is called for by the standards is simply not there. For example, something as simple as the number of authorized shares for companies whose legal system has this concept. Or, impairment. Under IFRS, the events and circumstances that cause recognition of an impairment loss are required to be disclosed. Many questions reference the company's disclosure of having taken an impairment charge, but the lack of this events and circumstances information. Other questions are in the consolidation and equity method area; information about why a particular method is used in unconventional fact patterns.

The second category of comments contains instances where the information appears to be included in the filing, but questions need to be asked in order to fully understand the disclosure. This could occur because some information is not explained properly, or is scattered throughout the filing. A good example of this was a comment to a registrant, the registrant's response to which was that a bit of information could be found by piecing together the contents of upwards of seven different footnotes. Examples like this contribute to the financial statements being difficult to understand for investors.

By "shallow" disclosure, I mean disclosure that is there, but really doesn't tell the investor anything. Revenue recognition policies are an example of this. Often the criteria for revenue recognition were taken straight from IAS 18 and listed as the registrant's revenue recognition policy. Is this what IAS 18's disclosure provisions call for? This information does not help a reader gain insight for an investment decision.

While I have covered presentation and disclosure you will note that I did not mention a third area; that is, the application of the accounting models themselves. This is because issues related to the actual application of an accounting model often are not point blank obvious from a read thru of the financial statements. Rather, the responses to questions about disclosures that are lacking can then lead to discerning that application issues are indeed present. As the SEC staff is still in the early days of its review process, I just

don't think we are to this point yet.

## What I Wonder

While my remarks have been around the factual nature of the types of questions the SEC staff has to-date asked, some of the registrant responses the SEC staff has received have acknowledged the validity of the points broached in the questions. Considering these responses brings me back to my "what I wonder as I wander" point. Again, what I wonder, as I wander, is the question of "why" what was done happened that way. In particular, is it first time jitters or long term perspective?

I suspect that first time jitters definitely played a part. I probably can't truly appreciate how difficult and draining it must have been for companies to establish a process to understand and implement a new set of accounting standards. For example, one registrant was most contrite when asked why its disclosure stated that it did "not" do exactly what a standard called for. The registrant replied that its accounting was right but that its footnote just contained one too many uses of the word "not." Luckily, first time jitters go away with continued learning and improvement of processes.

What about long term perspective? Is any part played by the notion that whatever the standard calls for — be it the principle or the words in the standard that go along with the principle — must be for the other person, but not for me? For example, the essence of the reply by a few registrants for whom particular disclosure seemed to be missing was along the lines of the fact that they just hadn't accumulated the information called for by the standard. While certainly it's good to know the reason, does this reflect a long term perspective on the stature of what the standards call for or a short-term data gathering problem?

## Closing

In closing, let me just say that I hope you find the information that I have tried to convey today — raw as it is — helpful. There seemed to be a demand for it, so I am happy to do what I can to contribute.

Lastly, let me leave you with a final thought which is to repeat the point in the "roadmap" that IFRS will be with us for a long time; so it is all the more important that we start out on the right foot.

Thank you very much for your attention.

*<http://www.sec.gov/news/speech/2006/spch121206jae.htm>*