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Dear Mr Maystadt,

## SHOULD IFRS STANDARDS BE MORE EUROPEAN?

### Mission to reinforce the EU's contribution to International Accounting Standards

Thank you for your letter of 2<sup>nd</sup> September and your invitation to comment on your draft report by 30 September 2013.

Standard Life Investments is a major global institutional investor with assets under management of Euro 208.7 billion as at 30 June 2013. Our clients are generally long-term investors. A significant proportion of the funds we manage are invested in the listed securities of European companies. In taking investment decisions on behalf of our clients, who are generally long-term investors, we rely to a significant degree on information prepared in accordance with international financial reporting standards ('IFRS') published by the International Accounting Standards Board ('IASB').

As reflected in the evidence I gave to you on 10 July, we are supportive of the IASB and its objectives but we have become increasingly concerned regarding its governance, due process and the very technical nature of its standards. This latter aspect is, we believe, very important because it has meant that many final users, particularly retail shareholders, of financial statements prepared in accordance with IFRS have been unable to cope with the sheer complexity of the technicalities of the standards. As a consequence many final users have disengaged from the standards setting process and it is proving very difficult for them to re-engage. This has led to serious questions as to whether financial statements prepared in accordance with IFRS are continuing to meet the need of the final users. In light of this, the way in which the EU contributes to the international accounting standard setting process and the governance pertaining thereto has become increasingly important in protecting the interests of the final users. Therefore, we believe it is essential that the EU's contribution is effective, robust and, importantly, takes account of not only the technical quality of the standards but also their implications for the long-term success of companies operating in the EU.

In the light of the above, we welcome the thrust of your draft report and the pragmatic approach you have taken to developing your recommendations and assessing the options, when appropriate. In the interests of efficiency let me convey concisely our comments on your recommendations, using the order and references in your draft report.

#### Your Recommendations

##### 2.1 Consensus on the commitment to global quality standards

We recognise and support the consensus to which you refer.

##### 2.2 Consensus on the maintenance of a 'standard by standard adoption procedure (with the possibility of accepting or refusing a standard produced by the IASB)'

We support the substance of your conclusion. In particular, we endorse strongly your view that 'prudence is essential', noting that prudence relates not only to the content of a standard but also to the way in which a standard is implemented by the preparers of financial statements and audited by the auditors. Our view on prudence is such that we would encourage you to harden your comments so that the issue of prudence and its primacy is re-examined by the IASB in light of the abuses of "neutrality", for instance through the use of incurred loss model

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provisioning and fair value accounting of unrealised profits. In making these comments we note the apparent reticence of the IASB, in their review of the conceptual framework, to reinstate the concept of prudence. We plan to make our views on the concept of prudence known to the IASB in replying to their discussion paper and would encourage you to strongly advocate it in your report.

Whilst we agree that 'the accounting standards adopted should not endanger financial stability', we suggest that this should be worded more positively, along the lines that 'the accounting standards adopted should promote financial stability'.

We support in principle the conclusion that EFRAG 'could be asked to analyse more thoroughly the compliance with the criteria regarding prudence and respect for the public interest'. We believe your conclusion would be strengthened by referring to 'the long-term public interest' thereby seeking to ensure due account is taken of short-term volatility that is sometimes created by accounting standards. Second, EFRAG could be asked to comment on the technical complexity of standards. We believe that such a measure, of itself, would make standard setters more cognisant of and responsive to the complexity issues. Hopefully, this might of itself lead to more simplicity of standards over time, thereby enabling final users and others to engage more effectively with the standard setting process.

### 2.3 How can the IASB be influenced? Who must advise the Commission on the adoption of the standards? Who must forward to the IASB the comments on the exposure drafts?

We support your preference for Option 1 with the following comments:

- We question why the national standards bodies need to be represented on the proposed 'high-level Board'. We believe that the national standard setting bodies should be engaging effectively and conclusively with the executive of EFRAG, with a view to ensuring that all recommendations to the high-level Board to approve comment letters and other matters enjoy the support of the national standards bodies at the time they are submitted to the Board. On this basis it should then be the responsibility of the high-level Board, comprising solely the European public institutions, the stakeholders and a President, to consider and, if appropriate, approve the recommendations. We believe that this would not only ensure more focussed and effective consideration of stakeholder and public interest issues but also avoid the discussions that take place at the high-level Board being dominated by technical issues, where the competence of the national standards setting bodies' representatives would make it difficult for the other members of the Board to challenge them and interact effectively.
- We have some empathy with the advantages you cite regarding increased influence being exercised by ESMA. That said, we are not convinced that in the short-term it would be sensible to transfer the attributions of the EFRAG to ESMA because of ESMA's perceived priorities and challenges, including resource limitations, for the foreseeable future. Therefore, we would encourage you to recommend that Option 2 be reconsidered in, say, 5 years' time. This would mean that the advantages to which you refer would remain on the radar and, furthermore, it would serve as an incentive to those involved with the recommended Option to ensure that it performs with a high degree of effectiveness.

### 2.4 The role of the ARC (Accounting Regulatory Committee)

We have no comments on this.

### 2.5 The European Parliament

We support your recommendation of setting up an 'early warning system' from the EFRAG to the parliament, noting that this could be effectively completed by the appointment of a permanent rapporteur for the IFRS, as you suggest.

### 2.6 The Monitoring Board of the IASB

We believe that the creation of an advisory group of standardisation specialists and final users, to advise the Commission on its participation in the Monitoring Board, is one of your most important recommendations. It will serve to enable final users to re-engage with effective authority with the IASB, recognising the pivotal influence and responsibilities of the Monitoring Board. We believe it would be important for the minutes and similar documents of such an advisory group to be available for public scrutiny in order that it can demonstrate that due regard for public interest issues. Furthermore, we encourage you to make explicit reference in your report to this advisory group having interaction in respect of the Monitoring Board's role in relation to the IFRS Foundation in order that this aspect of the group's responsibilities is not overlooked. We regard this as extremely important to ensuring that there is effective governance of the IASB.

Conclusion

We trust our views and comments will assist you in finalising your report, and we are grateful for your willingness to consider our comments on the important matters you are addressing.

In line with our usual practice, we shall be posting a copy of this letter on our website in due course.

Yours sincerely



Guy R Jubb  
Head of Governance & Stewardship  
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