Centre for Financial Market Integrity

CFA INSTITUTE

16 October 2007

Mr. Paul Pacter
IASB Director of Standards for SMEs
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Re: Exposure Draft –IFRS for Small and Medium-sized Entities

Dear Mr. Pacter:

The CFA Institute Centre for Financial Market Integrity (the CFA Institute Centre)[1] in consultation with its Corporate Disclosure Policy Council (CDPC)[2] appreciates the opportunity to comment on the exposure draft of proposed International Financial Reporting Standards (IFRS) for small and medium-sized entities (SMEs).

The CFA Institute Centre represents the views of investment professionals, including portfolio managers, investment analysts and advisors located in over 130 countries worldwide. Central tenets of the CFA Institute Centre mission are to promote fair and transparent global capital markets, and to advocate for investor protections. An integral part of our efforts toward meeting those goals is ensuring that the quality of corporate financial reporting and disclosures provided to investors and other end users remains of the highest quality. The CFA Institute Centre also develops, promulgates, and maintains guidelines encouraging the highest ethical standards for the global investment community through standards such as the *CFA Institute Code of Ethics and Standards of Professional Conduct.*

General Comments

The CFA Institute Centre does not support the IASB proposal to create a different set of reporting standards for SMEs. The views expressed by the lone dissenting board member in the

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1 The CFA Institute Centre for Financial Market Integrity is part of CFA Institute. With headquarters in Charlottesville, VA, and regional offices in New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 95,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 133 countries, of whom nearly 80,000 are holders of the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 135 member societies in 56 countries and territories.

2 The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The CDPC comprises individuals who are investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the CDPC provides the practitioners' perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

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alternative view section of the basis for conclusion align with our concepts on different standards: the proposed IFRS for SMEs would create non-comparable information. We present in the following pages the key reasons why we oppose different reporting standards based on ownership (public, private, nonprofit), size (small or large) or industry (financial or non-financial):

1. Investors make decisions by comparing alternative investments. Permitting an alternative accounting regime for companies that "do not have public accountability" ignores the following:

    - The growth of private equity as an investment class

    - The interests of bondholders and other creditors of "non-public" enterprises

2. To operate efficiently, capital markets require financial information that is: (a) comparable from firm to firm; (b) relevant to investment and financing decisions, (c) a reliable and faithful depiction of economic reality; and (d) neutral, favoring neither supplier nor user of capital, neither buyer nor seller of securities.

    - Transactions and economic activities that are similar should be reported similarly in financial statements. Alternative accounting for similar events may interfere with the integrity and usefulness of financial reports.

    - The potential timing lag between the adoption of new IFRS and their incorporation into "IFRS for SME" will result in further differences between the standards, causing increased difficulty in comparing large and small companies.

3. With the presence of various adopted forms of IFRSs—As issued by the IASB, as adopted by a national regulator, IFRS for SME—analysts may have a difficult time determining exactly which standards have been applied.

Private Equity Decision

While enterprises owned (wholly or in part) by private equity investors are not public enterprises in the conventional sense, they are different from enterprises that are wholly owned by managers. The information needs of the investors in such enterprises are no different from those of investors in public companies. Such investors must decide whether (and at what price) to make the investment, whether (and at what price) to make additional investments to fund capital requirements, and whether (and at what price) to sell their investment. Such decisions are usually made by comparing the subject enterprises with similar enterprises that are public. Such comparison is obstructed when the "nonpublic" company is permitted or required to use different accounting methods.

Bondholders and other creditors also require information to make sound lending decisions. Their information requirements do not differ because the enterprise lacks "public accountability." As in the case of shareholders, creditors generally compare the financial statements of prospective borrowers with those of similar public companies.

The information needs of investors and creditors are essentially the same, regardless of whether or not the enterprise has "public accountability." Some "nonpublic" enterprises are very large and engage in complex transactions (e.g. derivatives) similar to those engaged in by "public" companies. Exempting such firms from IFRS requirements may impair the efficiency of capital markets.

Comparability across Companies

The need for timely, relevant, complete, transparent, comparable, and consistent information is the foundation of Principle 1 in CFA Institute Centre's *Comprehensive Business Reporting Model* (CBRM).[3] Capital market participants use financial statement information to perform comparative analyses of companies' economic performance and financial position of business enterprises. Those analyses are the basis for estimating the company-specific valuations and assessments of future prospects that underlie informed and sound investment decisions.

While the draft IFRS for SMEs proposal was designed for companies without public accountability, there is no prohibition against national laws or regulations allowing or requiring companies to file using the new standards. It has been a long-standing position of CFA Institute that accounting and reporting standards should apply to all enterprises[4]. Regardless of whether the company has public accountability or not, everyone should account for and report similar economic activities and transactions in accordance with similar principles of accounting. With a single standard, applied as necessary by all types and sizes of companies, this difference would be limited and potentially eliminated.

Different Timing for Application

The proposal indicates scheduled updates to the IFRS for SMEs every other year, with special consideration allowed for significant accounting changes. This delay further demonstrates the difficulties produced by establishing dual reporting standards. Since most changes and additions will lag their application to public companies, creditors and other users of the general-purpose

[3] *A Comprehensive Business Reporting Model: Financial Reporting for Investors* (CBRM) contains twelve guiding principles to ensure that financial statements are relevant, clear, accurate and complete as companies communicate with current and potential providers of capital.
(http://www.cfainstitute.org/centre/cmp/BusinessReportingModel.html)
[4] Our 2001 comments to the Canadian Institute of Chartered Accountants on the topic of Differential Reporting is available on our website (http://www.cfainstitute.org/centre/issues/comment/2001/01diffrentl_report.html)

financial statements will have to maintain different knowledge bases and/or valuation models: one set for public companies and another for those classifieds as SMEs. A further wrinkle would appear if the SME moves forward with adopting the change made in the full IFRS before its inclusion in the update for similar companies. The potential for decreased comparability created by timing differences with multiple sets of standards would appear to outweigh the benefits of this proposal.

Transparency of the Set of IFRS Used

In companies' annual filings, they disclose the accounting principles applied to the values reported in the financial statements. In many cases, the reference is provided once with an abbreviation developed for future references. For example in the 2005 SEC 20F filing, AMVESCAP PLC provided in its Note 1 – Accounting Policies:

> *The Consolidated Financial Statements for the years ending December 31, 2005 and 2004 are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union and the Companies Act 1985, as amended (the "Companies Act")…*

On the face of the primary financial statement, they only indicate, "*Amounts in accordance with IFRS.*" The abbreviated use of "IFRS" as the sole description on the company's primary statement, while in fact applying different sets of standards, may lead to confusion. Investors and creditors may apply incorrect adjustments in their valuations when not properly informed by the company. An abbreviation for the set of IFRS used should sufficiently describe which set is being used by a company, e.g., IFRS-SME.

Closing Remarks

In conclusion, we strongly believe that different reporting standards will lead to the delivery of information that is not consistent with the requirements of Principle 1 of the CBRM. The non-comparable data creates additional complexities in analyses when coupled with the delay in applying new standards for SMEs by 12-24 months or longer. The board would be better served to focus on the development of proper guidance for the full IFRS requirements ensuring that all companies operating in a particular area (e.g. derivatives or joint ventures) can apply them. As the dissenting board member noted, "The vast majority of accounting policy decisions of an SME are straightforward and extensive reference to IFRSs will not be required and, when required, not burdensome."

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We appreciate the opportunity to comment on the International Accounting Standards Board's proposed IFRS for small and medium-sized enterprises. If you have any questions or seek elaboration of our views, please do not hesitate to contact Glenn Doggett, CFA, at +1 (434) 951-5278 or glenn.doggett@cfainstitute.org.

Sincerely,

/s/ Gerald I. White

Gerald I. White, CFA
Chairman of the CDPC
CFA Institute

/s/ Georgene B. Palacky

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