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Mr Fabrice Demarigny
Secretary General
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11-13 Avenue de Friedland
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15 January 2003

Dear Sir,

CESR CONSULTATION ON PRINCIPLES OF ENFORCEMENT OF ACCOUNTING STANDARDS IN EUROPE

PricewaterhouseCoopers welcomes the opportunity to participate in this important consultation on enforcement of International Accounting Standards (referred to for convenience in this letter using the new title 'IFRS') in the European Union. This response is submitted on behalf of the PricewaterhouseCoopers network of firms.

Introduction – support for principles-based standards of Enforcement

PricewaterhouseCoopers supports adopting principles-based standards for the enforcement of IFRS in the EU. Market regulation is an important part of the corporate reporting supply chain and, as other parts of that chain are increasingly defined by internationally recognised principles-based standards (for example accounting, auditing, corporate governance), we believe it is appropriate that the same should be true of market regulation standards. The setting of detailed rules on, for example, the structure of enforcement bodies, is not required. But investors and other market participants should be able to understand the standards of regulation that will generally apply across the EU and more widely, and expect that those will be applied in consistent fashion on a global basis.

In this regard we also support the principle of public accountability contained in the document – national regulators should not take a different view from their peers in other countries with regard to key enforcement issues, but if they were to do so that fact should be made public. To ensure transparency, regulators should be required to explain and justify their positions.

Need for global solutions

Achieving consistency in enforcement of IFRS at EU level will be a challenging and worthy goal. However many of Europe's largest companies operate on a worldwide basis, and some are listed on markets outside the EU. The IASB has already established IFRIC as a global interpretation body, but the greater challenge will be encouraging convergence of thinking by enforcers of accounting standards around the world. A useful first step would be to establish a formal requirement for coordination by the enforcement bodies in the largest capital markets that accept IFRS filings (for example, the EU, US and Australia.) CESRfin's Sub-committee on Enforcement, perhaps with the assistance of EFRAG, could assist by compiling the collective experiences in Europe for discussion with enforcement agencies from other parts of the world.

Pre-clearance and interpretations

We strongly concur with the view that enforcement actions should not be considered to provide interpretation of IFRSs. Matters should be referred back to the appropriate standards setting and interpretation bodies – otherwise there is the risk of creating GAAP without the opportunity for adequate due process. However, we recognise that pre-clearance occurs in certain circumstances and that pre-clearance decisions may be considered by the market to constitute official "interpretation". Further consideration is needed as to the appropriate degree of transparency around pre-clearance. Although greater openness in relation to general substantive disclosure and presentation matters would be welcome, it should be made clear that pre-clearance relates to particular company circumstances and is not necessarily indicative of the approach that should be taken in other cases. Also, there is a need for confidentiality where company results have not yet been announced to the market.

Detailed comments on Principles

We have not commented in detail on each of the 21 Principles set out in the consultation document, the majority of which we support. We have however commented below on specific issues, particularly where we consider the principles need to be more tightly drawn, or where certain issues are not covered by the principles. For convenience, these specific issues are summarised below:

- 'Financial information' needs to be better defined
- Criteria should be set for the skills, experience and resources of enforcers
- A requirement for enforcers to respond to third party complaints should be identified
- Further consideration is needed on access to information held by companies and auditors
- The principles should provide for an appeals process in the case of alleged infringements
- All national enforcement agencies, whether regulators or review panels, should participate in forums where coordination of enforcement is discussed

- Arrangements for enforcement responsibility in relation to cross-border listings and filings require further clarification
- Timeliness of public reporting should be considered

Scope of 'financial information'

Principles 1, 7 and 8 refer to 'financial information', being information provided by companies whose securities are admitted to trading on a regulated market, and where the information is "harmonised", such that EU legislation requires its publication and provides guidance on its format and/or content.

It is not clear whether the operating and financial review (OFR), or management discussion and analysis, provided in most listed company annual reports is covered by the definition. The OFR is clearly a document provided to investors by companies whose securities are traded on the capital markets, but is not at present the subject of any EU directive or other regulation as to its form and content. It is therefore unclear whether: firstly, enforcers should have a responsibility for the OFR and hence will be empowered to take action where information in the OFR is deemed misleading; and, secondly, whether enforcers should use the OFR as a source for their review of the financial statements.

This latter point is relevant because it may only be possible to assess the risk of problems attaching to the financial statements, if those statements are read in conjunction with the OFR. For example, trading conditions discussed in the OFR may alert reviewers to the possible existence of revenue recognition problems. It may be impossible to appreciate the existence of such problems by looking solely at the amounts in the profit and loss account.

Skills, experience and resources of enforcers

Competent authorities should be staffed by an adequate number of individuals having appropriate skill and experience in corporate reporting and market regulation. As the deadline of 2005 approaches, we would expect that staff conducting reviews would be expected to become familiar with the IFRS framework. This may require some retraining, or the hiring of additional staff with the requisite skills.

Moreover, the work of review staff should itself be subject to appropriate moderation and quality review. This may be achieved, for example, by having issues initially identified by staff subject to second review by a panel or individual with extensive practical experience, before any enforcement action is taken. An additional principle should be included in the document to cover these areas.

Finally, the resources available to the competent authority should reflect the size of the population of listed companies. More trained individuals will be required in, say, Germany and the UK, than in countries with smaller capital markets.

Trigger points for enforcement – third party complaints

The consultation paper gives the impression that enforcement action will normally only arise as a result of the competent authority's risk-based selection approach. We agree that the selection of company reports for examination should have regard to risk, including the size of the enterprise, industry type, and complexity of its operations and structure, and that this will provide the basis for the majority of enforcement action. However, we suggest that Principles 11-15 should also reflect the fact that there will be other events that should lead to companies becoming the subject of enforcement action. Authorities in some countries already have mechanisms for dealing with cases referred to them by other regulatory bodies, or complaints made by members of the public or by issues raised in the press.

Access to information from companies and auditors

Principle 5 states that the competent authority should have the power to "require supplementary information from companies and auditors". The primary responsibility for furnishing such information should fall on the officers of the companies concerned, reinforcing the principle of management responsibility for financial reporting. Where auditors are required by the authorities to provide additional information, this can usefully take the form of a report or, in special cases, a statement covering the specific issue raised by the relevant authority. This should be prepared by the auditor on the basis of specific additional work, drawing on the audit working papers and other relevant information considered by the auditor during the performance of the audit. Audit working papers serve to illustrate and evidence particular audit procedures and hence will generally not in themselves provide complete insight to the specific issue under discussion.

Auditors would seek to co-operate in enforcement actions, but would expect to act only at the request of the company in providing information to the competent authorities. Rules regarding client confidentiality differ between EU member states, and currently prevent the auditor from responding to information requests by third parties including national regulatory authorities.

Appeals process in the case of infringements

Principle 16 discusses the authority's ability to "take appropriate actions to achieve an appropriate disclosure and where relevant, correction of misstatement." However, there is no mention of a process of dialogue with the company to understand the issues surrounding a potential enforcement issue, nor of the right of appeal by the company (and its auditors) where enforcers take action. Companies and auditors should have the right to have their case heard before a final decision is made and before an action attracts any external publicity. The use of some type of review panel mechanism may be a good way of achieving this.

Involvement of review panels and regulators in coordination

The task of overall supervision and coordination of enforcement is assigned to CESR and its sub-committees. The membership of CESR formally comprises representatives of national securities regulators, however the principles recognise that various organisational models of enforcement are in place in member states, including enforcement by securities regulators, stock exchanges, and review panels. All national enforcement agencies should participate in forums where coordination of approaches to enforcement is discussed, irrespective of whether they are securities regulators or review panels.

Cross-border enforcement responsibility

We note that the Sub-committee on Enforcement is to draft further guidance on responsibilities in relation to cross-border listings and offerings. We agree that clarification is urgently needed as capital-raising becomes more geographically complex. For example, if a German company listed in Frankfurt also has secondary listings in London and Paris, do the Financial Services Authority or other UK competent authority and the COB in France have power to mount enforcement action as well as the German authority? One solution to this may be to route the responsibility for any enforcement action back to the relevant national regulator.

Moreover, should cases involving more than one EU territory be settled on a bilateral basis by the two or more national authorities involved? Or is the intention that such cases would have to be brought before CESR or a similar body comprising representatives of each national competent authority? We believe bilateral contact may lead to swifter resolution of an issue than bringing the matter before a group of 15 or more national representatives (set to increase to 25 after EU enlargement.)

Timeliness of public reporting

Principle 21 states "enforcers should periodically report to the public on their activities providing at least information on…decisions taken in individual cases". The implication from the text of this principle is that enforcers might only issue reports on an annual or other regular periodic basis. However we believe it will be important for key enforcement decisions to be made public as soon as is practicable. Although, as stated above, we believe enforcement actions should not be considered to provide interpretation of IFRSs, timely announcement of enforcement decisions may help other companies to avoid circumstances that may result in misstatement of financial information.

We would be happy to discuss our comments with you. If you have any questions regarding this letter, please contact Ian Wright in our London office (+44 20 7804 3300).

Yours faithfully,

PricewaterhouseCoopers