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Your ref

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Dear Mr Demarigny

Draft Standard No 2 on Financial Information – Coordination of Enforcement Activities

We appreciate the opportunity to respond to The Committee of European Securities Regulators (CESR) draft *Standard No 2 on Financial Information – Coordination of Enforcement Activities*. This letter expresses the views of KPMG International.

In these proposals and in Standard No 1 on *Financial Information: Enforcement of standards on financial information in Europe,* CESR has proposed a number of important principles that we support, including that:

- coordination of enforcement activity is desirable if consistency is to be achieved;
- coordination should encompass non-CESR bodies as this reflects the current EU approach to the regulation of national securities markets;
- enforcement should not lead to general interpretations being issued or to the creation of a parallel body of interpretations as this is role of the standard setting process;
- in a principles-based environment the application of reasonable judgment within those principles should not be 'second guessed' at a regulatory level; and
- the regime needs to be workable and that technological and innovative solutions should be adopted where this assists the objectives.

However, we believe that there are some elements of the proposals that should be reconsidered and improved.

Our key concern is that the regime must not lead to a rule-based interpretation and implementation of IFRS and relates to the organisation and content of the envisaged database.

The avoidance of a rule-based interpretation and implementation of IFRS will be a difficult objective to achieve and will require commitment from all parties. We believe that CESR shares this objective and we hope that this shared objective will make the comments and concerns expressed in the remainder of this letter useful to you.

As a final general comment and whilst we acknowledge the strenuous efforts of CESR in developing a coordinated approach to enforcement of IFRS in Europe, we note also that IFRS are not merely European Standards. We consider that any area which has implications for the interpretation of IFRS must be coordinated at a global level, consistent with the global nature of the standards.

Therefore we encourage members of CESR to elevate the discussion and debate to an IOSCO level at the earliest opportunity. Without the development of a broad consensus across IOSCO as to the appropriate method for consulting between enforcement bodies, there is a significant risk of the most active regulator determining the global interpretation and / or differing versions of IFRS developing through positions taken by different regulators. We do not consider either of these outcomes to be desirable.

Database

As noted above, we support the objective of coordination and, subject to confidentiality concerns (see below), we agree that the concept of a database may be an effective use of technology to facilitate consistency where time constraints preclude consultation between national enforcers before enforcement decisions are taken.

We understand why CESR proposes that both positive decisions (i.e., those that do not lead to enforcement action) and negative decisions (i.e., those that do lead to an enforcement action) should be included in the database.

However, we have some concerns about the inclusion of positive decisions, whether these decisions are ex-post or ex-ante. We have similar, lesser, concerns regarding the inclusion of ex-ante negative decisions.

First, in a principles-based environment, there will be a large number of (perhaps minor) variations on facts and circumstances that are dealt with appropriately by the same accounting treatment. To include on the database each of these acceptable variations in circumstances as they are encountered will lead to a significant increase in the number of database entries. This will make subsequent reference to the database more difficult (and slower).

Second, it is natural that greater consideration (and time) will be devoted to a negative decision and that such decisions will be the subject of far more rigorous due process. This is unsurprising

given the result of a negative decision, particularly in the case of ex-post decisions where the impact may be restatement. Accordingly, we consider that greater weight should be placed on negative decisions, particularly those that are determined ex-post.

We also are concerned that the inclusion of a large number of positive and negative decisions will lead to a rule-based approach. If the result of including positive clearance is a significant increase in the number of items on the database, the result is likely to become, in substance, a body of interpretative literature, which is contrary to the CESR principles. This is particularly dangerous were the database to be made public, in whole or in part, as is being considered.

Accordingly, we would support the construction of a database that includes ***only*** ex-post negative decisions. We consider that the inclusion of ex-ante negative decisions and positive decisions is acceptable only on the basis that they are included on a strictly confidential basis, for the information of the EU national enforcers only. Ex-post negative decisions should be clearly distinguishable from other decisions.

Confidentiality

We have considerable concerns about the confidentiality of consultation between EU national enforcers and the information retained on the database.

In the case of consultation between EU national enforcers, CESR will need to put in place a suitable, legally binding confidentiality regime if EU national enforcers are to consult in advance of decisions.

In the case of the database, our confidentiality concerns are particularly strong with regard to pre-clearance and positive findings, where information otherwise would not be in the public domain. We note that our concerns would be significantly reduced were the database restricted to negative findings related to ex-post decisions as the matter would be made public anyway e.g. through a revision of previously published accounts. Again, a suitable, legally binding confidentiality regime will be essential.

It is not clear to us that such a regime could be implemented simply through a Memorandum of Understanding (as suggested in the explanation to Principle 3) as it must be capable of surviving legal challenge if the appropriate protection is to be afforded to issuers.

Implementing measures

CESR's draft standard adds some detail to the principles set out in Principles 20 and 21 of Standard No 1 *Financial Information Enforcement of Standards of Financial information in Europe* and moves the EU a step closer to a consistent enforcement regime.

As the Foreword acknowledges, draft Standard No 2 is still an incomplete exposition of the planned regime – noting that it is a "principle-based standard establishing a framework that will

be completed by implementing measures necessary for the realisation of the identified principles."

In light of the short period of time between now and 2005 and the expectation that companies will publish IFRS-based information in advance of the 2005 deadline, it is becoming essential that the full extent and mechanism of CESR enforcement be developed.

Further, we are concerned that the proposals could fail were essential implementing measures subsequently found not to be practicable, eg confidentiality.

Accordingly, we believe that CESR should build quickly on the principles exposed to date and should undertake to expose all necessary implementing measures by 30 June 2004. We consider that it is important for CESR now to complete the proposals before further consultation rather than proceed further on a piecemeal basis.

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Please contact Mark Vaessen at 020 7694 8089 or David Littleford at 020 7694 8083 if you wish to discuss any of the issues raised in this letter.

Yours faithfully

KPMG