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Mr. Fabrice Demarigny
Secretary General
The Committee of European Securities
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11-13 Avenue de Friedland
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Our ref TH/288

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Dear Sir,

CESR's technical advice on a mechanism for determining the equivalence of the generally accepted accounting principles of third countries

We appreciate the opportunity to comment on the proposals. This letter expresses the views of the international network of KPMG member firms.

We support the definition of equivalence submitted by CESR to the European Commission in March 2007. We agree that equivalence should mean that investors are able to make a similar investment decision irrespective of whether they are provided with financial statements in accordance with IFRS as adopted by the EU (referred to subsequently in this letter as IFRS) or in accordance with a third-country GAAP. We also agree that market responses to accounting differences are particularly relevant in assessing the significance of such differences. We note, however, that it would be difficult to find a mechanism through which equivalence could be measured directly based on market responses, and so we support an approach which considers qualitatively, for each third-country GAAP, whether that third-country GAAP meets the definition of equivalence.

We agree that such an assessment should be made by the Commission, based on input by the third-country standard setter. We believe that CESR's proposal should recognise that equivalence is a two-sided coin. In other words, the stock exchange listing authority in a third country will often assess the equivalence of IFRS with third-country GAAP using a similar process to the one applied by the Commission. In our view, therefore, the mechanism should incorporate extensive consultation between the Commission and the third-country listing authority as well as with the third-country standard setter.

We also agree it is important that equivalence is assessed at a national level in principle for each third-country GAAP for which equivalence is sought, and that it should not be left for each company with a listing in the EU, or seeking such a listing, to determine the equivalence of its own financial statements, based on its own business model and its accounting policies, with the

information that it would report under IFRS. If the equivalence assessment, together with any remedies, were developed by each entity from scratch, then we believe the cost burden would increase significantly and at the same time it is doubtful whether a consistent application of the equivalence definition would be achieved.

However, we are concerned that one element of the mechanism proposed by CESR, the proposals for rectifying disclosures, may not be capable of meeting its objective. We note that the proposals use terms such as 'rectify' which could be taken to imply that a third-country GAAP is deficient or inferior to IFRS. We do not believe that this would often be the case. Rather, it will simply be that the two sets of principles have developed independently and have not since fully converged. Furthermore, anecdotal evidence suggests that informed investors take decisions to buy and sell shares in third-country registrants reporting under IFRS largely independently of the existence of additional reconciling disclosures. If this is the case, then we would question the usefulness of a requirement to develop and approve rectifying disclosures for each third-country GAAP for which equivalence is sought. We would suggest that either CESR or the Commission undertake further consultation with investor groups in order to determine what, if any, additional disclosures they would find necessary for a third-party GAAP to meet the definition of equivalence.

We note that equivalence does not mean that two GAAPs are identical in terms of measurement and disclosure principles, only that they are equivalent in terms of usefulness to informed investors. In our view, CESR should seek to develop principles that would assist the Commission in determining when two GAAPs should be accepted as equivalent without the need for additional disclosures. In order to do so, we would encourage CESR and/or the Commission to consult with representatives of informed EU investors. In the limited time available for comment, we have been unable to give proper consideration to how such principles might be drafted.

We are also concerned that the mechanism to develop rectifying disclosures may be complex and therefore burdensome for third-country standard setters to develop. In general, we believe that the resources of standard setters would be better spent on pursuing further convergence than on developing additional disclosures to rectify what may be short-term differences in principles. Instead, we believe that, wherever possible, an evaluation should be made that a third-country GAAP is equivalent, without additional disclosures, or that it is not equivalent. If it has not done so already, we would encourage either CESR or the Commission to consult directly with those third-country standard setters that may be affected most by the proposed mechanism.

Although we do not support the view that significant progress towards convergence with IFRS should be either the primary driver for, or a prerequisite for equivalence, in our view the existence of such a programme should be considered to be an important enabler for equivalence. A convergence programme on which significant progress has been made is likely to mean that significant measurement differences have been identified, and some of those differences have been removed. Depending on the outcome of further consultations with investor groups, it may

be possible to conclude that the remaining differences are well understood and that additional disclosures would not be considered useful by informed EU investors.

If the Commission determines that a third-country GAAP cannot be considered as equivalent without additional disclosures, then we could see merit in the proposal that the third-country GAAP might, in the short-term, be accepted as equivalent with additional disclosures. However, given our concerns about both the usefulness of additional disclosures and the cost of developing them, in our view the Commission should not encourage the third-country standard setter to pursue such an approach. Rather, we believe that the Commission should encourage the standard-setter to undertake or continue efforts to converge the third-country GAAP with IFRS.

The proposals imply that the disclosures required to remedy differences in measurement principles would need to be both 'non-complex' and more comprehensive than any form of reconciliation to IFRS. It is not clear to us what the form of such disclosures might be. In our view, if the proposal retains the notion that additional disclosures may rectify differences, then CESR should elaborate on the nature of the non-complex disclosures that it envisages.

We believe that CESR should further explain its proposal that measurement differences never could be overcome by any form of reconciliation to IFRS. In our view, if additional disclosures are considered to be useful at all, a reconciliation of the profit or loss and equity reported under the third-country GAAP to amounts that would be permitted under IFRS, supported by appropriate narrative descriptions, would be the most effective way to explain measurement differences to an informed investor.

Our further comments on the questions asked in the proposals are set out in the Appendix to this letter.

Please contact Mary Tokar at 0207 694 8288 or Terry Harding at 0207 694 8927 if you wish to discuss any of the issues raised.

Yours faithfully

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Appendix

Question 1: Do you agree that CESR's suggested method for handling applications for equivalence is the best way? In cases where the standard setter is not in a position to initiate and/or substantiate an application, do you have any concrete suggestions as regards the solution of such a situation and in particular, who could undertake the abovementioned assessments?

Generally, we agree that the standard setter for the GAAP in respect of which equivalence is being sought should be well placed to compare its own standards with EU IFRS. We find it difficult to envisage circumstances when a third-country GAAP could be sufficiently well developed to apply for equivalence and yet its standard setter would be unable to complete the process required for an application. However, if such circumstances were to exist, because of resource constraints, for example, then we suggest that the standard setter should be able to engage another party, such as the profession in that country, to carry out an assessment on its behalf.

Question 2: Do you think that CESR should publish guidance on the information that it would consider satisfactory to ensure an informed decision?

Not in detail. We believe that the nature of the information provided in support of an application for equivalence will vary significantly depending on the third-country GAAP being considered. In general each standard setter should be free to compile whatever information it believes would best support its application for equivalence. It may be helpful to standard setters, however, for CESR to provide a framework that describes the type of information that might be included in an application.

Question 3: Which of the two approaches indicated above (and in the Appendices) do you think is most appropriate?

See our response to question 4.

Question 4: Do you think the existence of a convergence programme should play any role in the determination of equivalence, other than facilitating the comparison between the standards and identifying the necessary rectifications?

As explained in the body of our letter, in general we support the approach proposed by CESR which focuses on the definition of equivalence. However, we expect significant progress under a convergence programme to be a major factor in ensuring that some differences have been removed and remaining differences have been identified and are well known to informed investors. In our view, the CESR proposal should place more emphasis on a process of convergence as an important enabler in achieving the requirements for equivalence without the need for additional disclosures.

Question 5: Do you agree that filters are important and that they should be reflected in any equivalence mechanism? If so, do you think the CESR model correctly reflects how consideration of the filters should be incorporated into the mechanism?

We agree that equivalence requires not only that the accounting recognition, measurement and disclosure principles are equivalent, but also that the third-country GAAP is supported by strong audit assurance and regulation. However, we note that these factors are important irrespective of whether an issuer's financial statements are prepared using its local GAAP, IFRS or a third-country GAAP.

Question 6: Do you agree with the proposal that any positive determination of equivalence by the Commission should be conditional on the standard setter in the third country agreeing to submit an impact assessment in respect of each new EU IFRS or third-country GAAP standard that is issued and to update any rectification disclosures as appropriate?

No. We believe the third-country standard setter should take on a less onerous obligation to report to the Commission on any changes in third-country GAAP that diverge from what would be permitted under IFRS or changes in IFRS that are not expected to be incorporated into third-party GAAP and which, in the view of the national standard setter, are so significant that equivalence should be reconsidered. We assume that the need to report to the Commission under such a regime would be uncommon in a country in which a convergence work programme is underway.