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**CESR work to date in relation to the European Commission's measures on the use of third countries' GAAP in the EU**

**I. Background information**

1. The European Commission's measures on the use by third country issuers of information prepared under local or internationally accepted accounting standards was published on the Official Journal of the European Union on 5 December 2006 (Commission Regulation 1787/2006 of 4 December amending Commission Regulation 809/2004 on prospectuses and Commission Decision 2006/891/EC of 4 December 2006 on the use by third country issuers of securities of information prepared under internationally accepted accounting standards). Both texts are published at the CESR's website.
2. These measures envisage a different treatment of such issuers before and after January 2009:
  - First phase: transitional period until January 2009. During this phase, accounting frameworks other than IFRS, Canadian, Japanese or US GAAP may be used subject to certain conditions<sup>1</sup>. The decision to accept other accounting frameworks is the responsibility of the competent authority, although recitals in the two measures state that *"To ensure consistency within the Community, CESR should co-ordinate the competent authorities' assessment as to whether those conditions are satisfied in respect of individual third country GAAPs"*
  - Second phase: after the transitional period, a third country's GAAP will be acceptable only if it has been determined equivalent to IFRS by the European Commission pursuant to their definition of equivalence which they will establish by 1 January 2008. The Commission will consult CESR on the appropriateness of the definition of "equivalence", the "equivalence mechanism" and the actual determination of the equivalence.

**II. Phase I**

**A. Mapping out the main third countries' GAAP used by issuers with securities admitted to trading on a regulated market in the EU (other than Canadian, Japanese and US issuers).**

3. CESR has drawn up a list of all the GAAPs used by third country issuers with securities admitted to trading in the EU.
4. CESR also investigated whether the GAAPs used by the majority of those issuers (over 90%) could be considered to satisfy the EC's revised transitional criteria. The conclusion of this work is summarised in the following table:

<sup>1</sup> According to Article 35.5A (c) of the Prospectus Regulation (and the similar provision in the Transparency Decision) these conditions are:

- (i) The third country authority responsible for the national accounting standards in question has made a public commitment, before the start of the financial year in which the prospectus is filed, to converge those standards with IFRS;
- (ii) That authority has established a work programme which demonstrates its intention to progress towards convergence before 31 December 2008; and
- (iii) The issuer provides evidence that satisfies the competent authority that the conditions in (i) and (ii) are met.

Art 35.5A (a) of Prospectus Regulation (PR)	Issuers from these countries should be able to include in the notes to the financial statements a statement of compliance with IFRS, as these countries have adopted IFRS.	<ul style="list-style-type: none"> <li>- Australia</li> <li>- Hong Kong</li> <li>- New Zealand</li> <li>- South Africa</li> <li>- Singapore</li> </ul>
Art 35.5A (a) or (b) of PR	These countries do not have “national GAAP” as such and their issuers apparently apply US GAAP, IFRS or Canadian GAAP.	<ul style="list-style-type: none"> <li>- Cayman Islands</li> <li>- Bermuda</li> <li>- Netherlands Antilles</li> <li>- Isle of Man</li> <li>- Jersey</li> <li>- Guernsey</li> <li>- British Virgin Island</li> </ul>
Art 35.5A (c) of PR	The countries on the right could qualify for letter (c) as CESR found that there is a public statement of a convergence programme.	<ul style="list-style-type: none"> <li>- Taiwan</li> <li>- China</li> <li>- Brazil</li> </ul>

5. CESR has decided to follow this research up by carrying out further work in relation to those countries that appear to be able to comply with the conditions under letter (c) of Article 35.5A of the PR or Article 1 (c) of the Transparency Decision (a public commitment to converge with IFRS and a work programme). Accordingly CESR-Fin will send letters to the national standard setters of Brazil, China and Taiwan asking them to provide further information on the nature of the convergence programmes they have established. Any findings arising out of this further work will be shared with CESR Members at a later date.

6. The decisions contained in the table above will not prejudice the possibility that other third countries might be found to comply with the transitional provisions in future.

**B. Development of a list of criteria that competent authorities will follow to determine whether the accounting principles of a third country -Art. 35.5A (c)- fulfil the required conditions to be accepted**

7. CESR has sought to define two key terms contained in the Commission’s equivalence measures, both of which it has used in establishing which countries should be included in the table above.

- **A public commitment to converge with IFRS**

The commitment should have been made by a senior official of the national standard setter (NSS) acting in that capacity. A statement will be considered "public" when:

- it has been made available on the website of the NSS or has been disseminated through another similar publication mechanism designed to make the information available both within the standard setter's local community and internationally; and
- it has been made available on IASB’s website; or
- it has been communicated to CESR or the European Commission.



- **A work programme which demonstrates an intention to progress towards convergence before December 2008**

A convergence programme which demonstrates an intention to progress towards convergence is a convergence program which is aimed at eliminating differences between the local GAAP and IFRS by 31 December 2008.

**C. Exchange of information between CESR members concerning decisions to accept (or reject) third countries' GAAP**

8. CESR members may need to take two types of decisions in relation to third country GAAP following either Article 35.5A (c) of the Prospectus Regulation or Article 1 (c) of the Transparency Decision:
  - Approval of prospectuses including financial statements produced under a local GAAP, if the third country issuer is making a public offer of securities in an EU Member State or applies for the admission to trading of its securities to a regulated market within the EU; and
  - Acceptance of financial reports including financial statements produced in a local GAAP if the third country issuer has securities admitted to trading on a regulated market ("financial reports" include both annual and half-yearly financial reports in cases where the third country issuer has equity or debt securities admitted to trading on a RM).
9. The first competent authority to receive an application for acceptance of a GAAP under Article 35.5A (c) of the PR or Article 1 (c) of the Transparency Decision should decide the acceptability of that GAAP using the criteria set out above. Since any decision on the acceptability of a GAAP under article 35.5A(c) made by one competent authority will, from a consistency angle at least, work to bind others, CESR members should inform the CESR Secretariat which GAAPs they intend to allow under this article as soon as possible in the decision making process. This will then allow the Secretariat to inform other members which GAAPs are being accepted so that contradictory or inconsistent decisions can be avoided. Consultation with other CESR Members prior to the acceptance of a GAAP is encouraged where possible. The CESR Secretariat should also inform CESR members as quickly as possible when a third country notifies CESR or the EU Commission that it has established a convergence programme such that it can satisfy the requirements for a public statement detailed above.
10. Subsequently, the case will be included in the agenda of the next EECS meeting, as an information point.
11. Finally, any decision on the acceptability of a GAAP under article 35.5A(c) of the PR or Article 1 (c) of the Transparency Decision made by one competent authority under the transitional provisions will not act to prejudice any future decisions on equivalence that might arise out of or subsequent to CESR's assistance to the EC in determining an equivalence mechanism.
12. Moreover, CESR might inform the Commission of any reservations it might have on GAAPs accepted under the transitional provisions under any eventual definition of equivalence arrived at during phase 2 of this exercise.

**D. Enforcers that are not CESR members**

13. Those Member States that have appointed a competent authority to examine that the financial statements are drawn up in accordance with the relevant reporting framework and to take appropriate measures in case of discovered infringements that is not the CESR



Member for that country, will establish appropriate arrangements with those authorities in order to ensure compliance with the commitments under this report.

### **III. Phase II**

14. CESR has submitted on 6 March 2007 to the European Commission its advice (07-138) in response to the first Commission's request received on 22 February. In this first report CESR has provided:

- a) A list of all GAAPs used by third country issuers that are traded on an EU regulated market in order to assess the current situation in the EU. This list will also include the number of issuers that are using each of the GAAPs concerned.
- b) A definition of equivalence that will be used for determinations of equivalence.
- c) A report on the progress made so far by Japan and US in their convergence towards IFRS. This will not include any evaluation of these convergence programmes. We will also confirm whether Canada will adopt IFRS in 2009.

### **IV. Interpretation of the measures on equivalence**

15. The paragraphs below set out CESR's understanding of the current situation regarding acceptance of third country GAAPs both during and after the transitional period including who is entitled to take both types of decision.
16. A determination of equivalence can only be made by the European Commission. Although individual CESR members as competent authorities can accept financial statements or approve prospectuses which include financial statements prepared in accordance with equivalent third country GAAPs (cf. Article 23 of the Transparency Directive and Article 20 of the Prospectus Directive), it is in CESR's view that such GAAPs should only be accepted by the competent authorities if the Commission has previously determined that such GAAPs are equivalent to IFRS (cf. Article 35.5E of the Prospectus Regulation and Article 2.5 of the Transparency Decision). As envisaged in these two measures, the Commission will determine equivalence after consulting CESR on the definition of equivalence, the equivalence mechanism and any determinations of equivalence.
17. The Commission must ensure a determination of equivalence of third country GAAPs has been made at least six months before 1 January 2009. In the interim period from 1 January 2007 to 31 December 2008, the Commission has adopted the two equivalence measures mentioned above.
18. During this interim period, competent authorities can accept GAAPs other than IFRS, Canadian, Japanese or US GAAP on the basis that the requirements of Article 35.5A(c) of the Prospectus Regulation (see footnote 1) or the parallel provision in Article 1 (c) of the Decision on Transparency are met. As described in section II.B of this report, CESR has developed a list of criteria for competent authorities to follow in making such decisions with a view to facilitating a consistent approach by all CESR members. These are not to be considered decisions on equivalence and will not prejudice the EC's future decisions on equivalence. The rationale behind allowing this transitional period is to give more time to the EC and CESR to assess the degree of convergence of certain GAAP towards IFRS in preparation for the future determination of equivalence that the EC will adopt when the transitional period expires.

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