

European Securities and Markets Authority (ESMA)

Stockholm, 10 October 2013

## Consultation Paper: ESMA Guidelines on enforcement of financial information

Representing preparers' point of view, the Swedish Enterprise Accounting Group (SEAG) welcomes the opportunity to comment on the Consultation Paper.

### Summary

The enforcement of financial information plays an important role in contributing to a high quality financial reporting providing a fair presentation of the reporting entity. We believe that it is wise to make use of the enforcement experiences up to date and revise the Guidelines (previously Standards) based on identified needs.

We strongly support the work on harmonization conducted by ESMA and would wish for the global harmonization on enforcement to develop the same way. We are convinced that ESMA plays an important role in this aspect and we would expect ESMA to also direct the appropriate level of resources from its funding towards the work on global harmonization.

Furthermore, we support the activities of the European Enforcers Coordination Sessions (EECS) and the publication of enforcement decisions on an anonymous basis. We appreciate that ESMA include a statement in the Guidelines on the important distinction between standard setting/interpretation/application guidance on one hand and enforcement on the other (paragraph 41) and we would expect this distinction to be well established within ESMA going forward, especially on the point that application guidance is within the authority of the standard-setter. Any diverging individual opinions within ESMA on this important subject are simply not acceptable. In this context we also want to emphasize the importance of making reference to materiality and fair presentation based upon relevant, reliable, comparable and, last but not least, understandable information. The Guidelines lacks reference to fair presentation and its building blocks.

Supporting the overall objective of the Guidelines, we would nonetheless like to bring specific parts of its content to your attention, were we do not share your view:

- We do not see the rationale for not keeping selection models public. We believe that enforcement priorities made public is the most effective way to enhance quality in line with the objective of enforcement. We are also convinced that ESMA will gain confidence in keeping its activities as transparent as possible.
- On the important subject of enforcers' independence, we do not agree that there is, per default, a conflict of interest and an independence issue when delegating the enforcement to regulated market operators. We have not had reasons to question the Swedish enforcement model, set up this way, from an independence perspective.

- We note the frequent reference to “avoiding regulatory arbitrage”. In the introduction and the objective of the Guidelines it is given equal prominence to “investor’s confidence in financial markets” and “consistent application of IFRSs”. We question to what extent regulatory arbitrage is an existing problem and ask ESMA to reconsider the reference to it.
- The examination procedures include the activity of posing questions to or having meetings with the auditors, which is reiterated from the Transparency directive. We urge ESMA to clarify in its Guidelines that the communication from the enforcer should primarily be directed towards the issuer of the financial information, who may in turn involve its auditors. It should only be in the absence of collaboration from the issuer that the enforcer may turn directly to the auditors.

Please refer to the Appendix for our answers to a selection of the specific questions stated in the Guidelines.

We are pleased to be at your service in case further clarification to our comments will be needed.

Yours sincerely,

CONFEDERATION OF SWEDISH ENTERPRISE



Dr Claes Norberg  
Professor, Director Accountancy  
Secretary of the Swedish Enterprise Accounting Group

*The Swedish Enterprise Accounting Group (SEAG) represents more than 50 international industrial and commercial groups, most of them listed. The largest SEAG companies are active through sales or production in more than 100 countries.*

## Appendix

### Question 1

*Do you think that the proposed Guidelines will improve the quality and consistency of financial reporting in Europe?*

We find the question difficult to answer since few references are made to the EU legislation that forms the starting point for the proposed Guidelines as well as to the current CESR Standards. A table of concordance would have been helpful to assess what amendments that are proposed.

Having said that, we strongly support efforts to ensure an efficient enforcement in all Members States carried out in a similar way, thereby ensuring a level playing field for all preparers.

### Question 2

*Do you have any comments on the potential costs to the financial reporting community of any aspects of these proposals?*

We find the question difficult to answer. We also find it surprising that no cost-benefit analysis has been performed based on the argument that the Guidelines are not addressed to financial market participants. This assessment is erroneous since it is preparers that are the target for enforcement and preparers of course will bear a cost (implicit or explicit) for enforcement. The issue is what the total cost is for an effective European enforcement system that secures a level playing field and what the benefits are. We urge ESMA to perform such an analysis before the Guidelines are adopted since we believe that no decision reasonably can be taken without having an idea of what the effects are.

### Question 3

*Do you agree that a common European approach to the enforcement of financial information is required in order to avoid regulatory arbitrage by issuers? In this context, regulatory arbitrage refers to the position where an issuer's choice of the market on which to list its securities may be influenced by different approaches to enforcement be applied in different European jurisdictions.*

In the draft numerous references are made to regulatory arbitrage. We quite frankly wonder if ESMA has detected any such cases and if so, how many. To us it seems like a theoretical problem. We ask for evidence regarding this phenomenon that we suspect cannot really be a big issue. We therefore urge ESMA to delete this from article 1 (purpose) of the draft Guidelines and the other articles where this reference is made, unless ESMA can present evidence that such arbitrage has been a common problem.

### Question 5

*Do you agree that issuers from third countries using an equivalent GAAP to IFRS should be subject to an equivalent enforcement and coordination system? Do you agree with the measures proposed to make this enforcement more efficient?*

Yes, we agree that issuers from third countries using an equivalent GAAP to IFRS should be subject to an equivalent enforcement and coordination system

### Question 6

*Do you agree that enforcers should have the powers listed in paragraph 30 of the proposed Guidelines? Are there additional powers which you believe that enforcers should have?*

The powers listed in paragraph 30 are reiterated from the Transparency directive and thus not subject to comment or change in this process. Instead we believe that they could be further clarified in the Guidelines, which is partly done in paragraph 54 concerning examination procedures. Please refer to our answer to question 14 for comments connected to the right to require any information and documentation relevant for enforcement from the auditors of the examined issuer.

### Question 7

*Do you agree that enforcers should have adequate independence from each of government, issuers, auditors, other market participants and regulated markets? Are the safeguards discussed in paragraphs 38 to 41 of the proposed Guidelines sufficient to ensure that independence? Should other safeguards be included in the Guidelines? Do you agree that market operators should not be delegated enforcement responsibilities?*

We agree that it is important that enforcers have adequate independence from various stakeholders and we agree with the principles set out in the proposed Guidelines apart from the proposal to prohibit market operators. Prohibiting market operators from assuming delegated enforcement responsibilities is according to our understanding only going to affect Sweden, being the only country within the EU having this structure today. Our experience is that independence from the market operator has not been an issue with this set-up for enforcement in Sweden. Adding to this, the market operators are under supervision from financial market authorities. Our conclusion is therefore that a prohibition might be too far-reaching.

Adding to this, we would like to point out that it is important that an enforcer have sufficient resources and the competence to perform assessment of financial reports. Independence in itself does not guarantee high quality enforcement.

**Question 8**

*Are you in favor of enforcers offering pre-clearance? Do you have any comments on the way the pre-clearance process is described and the pre-conditions set in paragraph 42 to 45 are described?*

To our knowledge there is no extensive demand for pre-clearance among Swedish companies and we do not wish for such a development in our jurisdiction. Contrary, we fear that should the enforcers be obliged to offer pre-clearance it may create a process that we do not see today in Sweden and would not wish for the future.

**Question 10**

*Do you agree that a risk-based approach to selection should not be used as the only approach as this could mean that the accounts of some issuers would potentially never be selected for review?*

Yes, we agree that a risk-based approach should be combined with a rolling scheme to capture all issuers over a certain time period. We believe that the system that has been used by the Swedish enforcer has worked well in this sense.

**Question 11**

*Do you agree that the risk-based approach should take into account both the risk of an individual misstatement and the impact of the misstatement on financial markets as a whole?*

Yes, we agree.

**Question 12**

*Do you think that a maximum period should be set over which all issuers should have been subject to at least one full review (or to be used to determine the number of companies to be selected in sampling)?*

Yes. See also our answer to question 10.

**Question 13**

*What are your views with respect to the best way to take into account the common enforcement priorities established by European enforcers as part of the enforcement process?*

We disagree with what is stated in article 52 of the draft Guidelines. We believe contrary to ESMA that selection models should be made public and we do not understand the argument that they should be kept secret “because of their nature”. We believe that enforcement activities are aiming to influence behavior. Therefore also selection models and what areas enforcers are targeting should be made public. The idea of secret selection models and inspections to check compliance afterwards seems somewhat “old-fashioned” in the world of fast flowing financial information.

#### Question 14

*Do you agree that the examination procedures listed in paragraph 54 of the proposed Guidelines are appropriate for an enforcer to consider using? Are there other procedures which you believe should be included in the list?*

We understand that the enforcer would need to have the power to contact the auditor on a certain matter in a situation where the issuer refuses to answer questions from the enforcer or does not collaborate to the extent it is required. We also acknowledge that it may be common for certain issuers to involve the auditor in a discussion with the enforcer. This should always be on the initiative of the issuer as long as the issuer is collaborating with the enforcer. We strongly object to a possibility for the enforcer to turn directly to the auditor without involving the issuer, unless required by the situation. We ask ESMA to clarify the power of paragraph 54 c) in accordance with this view.

#### Question 15

*Do you agree that, in determining materiality for enforcement purposes, materiality should be assessed according to the relevant reporting framework, e.g. IFRS?*

Yes, we strongly agree. It is important that the enforcer safe-guard this principle so that there are no generic expressions on how to determine materiality in the Guidelines or in the submissions of decisions or emerging issues to the EECS database, which goes beyond the materiality principles as expressed in IFRS.

We also expect the enforcer to keep reference to the fair presentation of the issuer's financial position, performance and cash flows and to promote the issuer's efforts to present information in a manner that provides relevant, reliable, comparable and understandable information. In order to arrive at providing relevant and understandable information in particular, a strict so called "check-list"-procedure conducted by the issuer, auditor or enforcer may be devastating. The Guidelines do not make direct reference to the concept of fair presentation and importance of providing relevant, reliable, comparable and understandable information. It is a weakness, since these features are key in assessing the quality of financial reporting and the compromises needed in order to fulfill these features.

#### Question 20

*What are your views about making public on an anonymous basis enforcement actions taken against issuers?*

We support a continued process of making public enforcement actions taken against issuers on an anonymous basis. We appreciate that the cases are described in detail as such presentation mitigates the risk for misinterpretations. The actions made public should not contain any interpretation of the standards that goes beyond what can be read out in the IFRSs themselves or accompanying conclusions published by the IASB. It is of utmost importance that the roles of standard-setting and enforcement are kept apart.