CENTER FOR AUDIT QUALITY
Serving Investors, Public Company Auditors & the Markets

October 15, 2010

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: File No. 4-608 – Notice of Solicitation of Public Comment on Consideration of Incorporating IFRS into the Financial Reporting System for U.S. Issuers

Dear Ms. Murphy:

The Center for Audit Quality (CAQ) is an autonomous public policy organization dedicated to enhancing investor confidence and public trust in the global capital markets. The CAQ fosters high quality performance by public company auditors, convenes and collaborates with other stakeholders to advance the discussion of critical issues requiring action and intervention, and advocates policies and standards that promote public company auditors' objectivity, effectiveness and responsiveness to dynamic market conditions. Based in Washington, D.C., the CAQ is affiliated with the American Institute of Certified Public Accountants (AICPA). The CAQ appreciates the opportunity to respond to the U.S. Securities and Exchange Commission's (SEC or the Commission) *Notice of Solicitation of Public Comment on Consideration of Incorporating IFRS into the Financial Reporting System for U.S. Issuers* (the request for comment or notice). This letter represents the observations of the CAQ, but not necessarily the views of any specific firm, individual or CAQ Governing Board member.

The CAQ believes that investors would benefit if issuers around the world prepared financial statements using a single set of high-quality accounting standards as noted in the CAQ comment letter[1] on the SEC's *Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers* (the Roadmap). International Financial Reporting Standards (IFRS) have proven to be a high-quality set of standards for preparing transparent financial information and are well positioned to be the set of globally accepted accounting standards. The February 24, 2010 Commission statement[2] in support of convergence and global accounting standards directed the SEC staff to develop and execute a work plan to consider specific areas and factors,

[1] http://www.thecaq.org/newsroom/pdfs/CAQCommentLetter-IFRSRoadmap.pdf
[2] http://sec.gov/rules/other/2010/33-9109.pdf

including the topics noted in the request for comment, before potentially transitioning the current financial reporting system for U.S. issuers to a system incorporating IFRS. The CAQ encourages the SEC to continue execution of the work plan to enable the Commission to be in a position to make a final decision in 2011 whether to incorporate IFRS into the U.S. financial reporting system. Assuming the Commission affirmatively decides to incorporate IFRS in 2011, we believe issuers first time reporting under IFRS (i.e., opening balance sheet date under IFRS) should be no earlier than 2015 or 2016, in order to allow adequate time to appropriately address implementation issues to achieve a smooth transition to IFRS in the United States as discussed in further detail below.

We support the SEC's solicitation of public comment as part of the SEC staff's execution of the work plan to better inform its ongoing consideration of incorporating IFRS into the financial reporting system for U.S. issuers. However, we are concerned that a 60 day comment period may not allow sufficient time for U.S. issuers and other stakeholders to prepare comprehensive responses to the request for comment for the Commission's consideration.

The CAQ acknowledges that the SEC's request for comment was primarily targeted at issuers. However, we believe the observations provided within this letter, which draw upon the collective experiences of members of the public company auditing profession, are relevant to many of the issues raised in the request for comment. Further, we note the request for comment poses specific questions in regards to the effect incorporation of IFRS into the U.S. financial reporting system would have on audit committee members serving in a financial expert role as well as an issuer's ability to comply with quantitative securities exchange listing requirements. To best inform the work plan process, we encourage the SEC to conduct targeted outreach as follows:

- *Audit Committee Financial Experts* - In regards to corporate governance requirements, the extent to which audit committee members will meet the SEC financial expert definition (and other exchange listing requirements) under an IFRS reporting requirement will vary by company. For example, those individuals serving on the audit committee of large multi-national companies, as compared to smaller U.S. issuers, may have more familiarity with IFRS due to the IFRS statutory reporting requirements for the company's international subsidiaries. As such, we believe this outreach should ensure a broad cross-section of audit committee representatives (i.e., those that serve on the audit committees of large multi-national companies and smaller domestic companies) either directly or through collaboration with representative organizations (i.e., National Association of Corporate Directors, Association of Audit Committee Members, Inc., etc.). We believe the feedback obtained from those individuals serving smaller U.S. issuers with potentially less familiarity with IFRS may provide valuable observations and unique insights into the specific challenges faced from the smaller company perspective in regards to incorporation of IFRS.

- *Securities Exchanges* - In order to best evaluate potential challenges that incorporation of IFRS may present we recommend that the SEC work closely with the individual securities exchanges to identify potential issues and determine the appropriate course of action to address such issues, including potential modifications to the rules governing listing securities on the exchanges.

We have a number of general observations in response to aspects of the request for comment which are presented below for the Commission's consideration:

- Transition or Phase-in Period
- Contractual Arrangements
- Corporate Governance
- Securities Exchange Listing Requirements

Transition or Phase-in Period

We note that the experiences of other countries that have adopted or are in the process of adopting IFRS demonstrate the need for sufficient preparation time in making the transition to IFRS within the United States. Prudent companies will want to have the appropriate processes and systems in place prior to the date of transition (i.e., the beginning of the earliest period presented in the company's first IFRS financial statements). A transition or phase-in period will allow issuers sufficient time to appropriately plan and effectively assess the impact of IFRS incorporation on their accounting policies, internal processes and controls, regulatory and statutory reporting, technology infrastructure, and other issues such as contractual commercial arrangements, compliance with corporate governance and related disclosure requirements, compliance with quantitative stock exchange listing standards, and the application of statutes governing sales of assets.

The SEC statement in support of convergence and global accounting standards notes that in 2011, assuming completion of the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) convergence projects and the staff's Work Plan, the Commission will determine whether to incorporate IFRS into the U.S. financial reporting system. According to the statement, the first time that U.S. companies would be required to report under such a system would be approximately 2015 or 2016.

Consistent with this timing, we note a recent AICPA IFRS Readiness Survey[3] (AICPA IFRS Survey) conducted in May 2010 found that of the 596 U.S. public companies surveyed, 56% believe that first time IFRS reporting in 2015 or 2016 would allow sufficient time to adequately prepare for IFRS adoption ***if*** the SEC determines in 2011 to require the use of IFRS for U.S. public companies.

We support the proposed timing and believe the Commission should allow 18 to 24 months between the point at which it decides to require mandatory transition to IFRS and the date of transition (i.e., opening balance sheet date under IFRS). Further, the transition process could be assisted if the Commission reduced the requirement for comparative financial statements to one year in a registrant's initial implementation of IFRS.

Contractual Arrangements

Incorporating IFRS into the U.S. issuer financial reporting system may affect the application, interpretation, or enforcement of contractual arrangements. However, the CAQ believes that the impact IFRS incorporation may have on contractual arrangements may be somewhat alleviated by progress on convergence between IFRS and U.S. Generally Accepted Accounting Principles (U.S. GAAP). While converged standards (i.e., leasing, revenue, financial instruments) will reduce the effect incorporation of IFRS will have on compliance with contractual agreements, preparers of the financial statements will nonetheless need to evaluate contractual terms to avoid potential unintended consequences. Importantly, however, this is not a new process as this is similar to the efforts undertaken by preparers today when any significant new accounting standard is adopted into U.S. GAAP.

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[3] *IFRS Readiness Tracking Survey*. AICPA. May 2010. http://www.aicpa.org/Research/StudiesandPapers/DownloadableDocuments/IFRS%20Readiness%20Survey%20--%20May%202010%20--%20Public.pdf.

The Commission notice questions whether U.S. issuers would treat the incorporation of IFRS differently compared to the treatment of a change in existing standards under U.S. GAAP. We note that the FASB has revised standards over time and as a result, U.S. issuers have processes in place to manage continued compliance with contractual arrangements (i.e., debt covenants, capital contributions, share-based payments). Certain contractual arrangements are based on U.S. GAAP provisions or requirements in place when the arrangements were initially executed (i.e., "frozen" U.S. GAAP provisions). In this circumstance, issuers have processes in place to capture financial information utilizing current U.S. GAAP, which changes over time for financial reporting purposes, and "frozen" U.S. GAAP, for purposes of evaluating and reporting compliance with contractual arrangements. Alternatively, other contractual arrangements may be based on current U.S. GAAP. For arrangements using current U.S. GAAP, issuers also have processes in place to manage the impact of changes in U.S. GAAP (resulting from routine standard-setting) on their financial reporting and compliance with contractual provisions. The CAQ believes that incorporation of IFRS will likely be treated by U.S. issuers in a manner similar to the processes noted above for determining compliance with arrangements based on current or "frozen" U.S. GAAP. However, we acknowledge that U.S. issuers are typically only required to adapt to a manageable number of discreet changes to U.S. GAAP in any given year. Given the broad scope of IFRS incorporation, this will require issuers to examine all of their contractual arrangements which may result in more arrangements being affected at one time. Therefore, as stated above, a sufficient transition or phase-in period will provide issuers with time to understand the impact that IFRS incorporation would have on the financial statements, contractual arrangements and the planning for other business activities (i.e., mergers and acquisitions). An understanding of this impact will allow issuers to determine an appropriate course of action to address such issues by amending agreements or renegotiating terms prior to the IFRS effective date.

Corporate Governance

The Commission's notice observes that the incorporation of IFRS into the U.S. financial reporting system may affect compliance with corporate governance and related disclosure requirements applicable to U.S. issuers. Specifically identified is the impact that incorporating IFRS may have on the role of the audit committee financial expert. The CAQ offers the following observations in regard to this issue:

- Given the periodic changes to U.S. GAAP, financial experts are currently faced with the challenge of educating themselves and understanding the implications such changes may have on the issuer and their continuing designation as an audit committee financial expert. However, we acknowledge that incorporation of IFRS could more significantly affect the financial expert role due to the broad-based scope of this change as opposed to a discreet change in U.S. GAAP in any given year.
- The CAQ believes that the potential impact incorporating IFRS may have on audit committee financial experts is partially dependent upon, and may be reduced by, the progress made by the FASB and IASB on the projects included in the Memorandum of Understanding.
- Large, multi-national companies may be better positioned to fill the financial expert role given that a number of audit committee members will already have familiarity with IFRS, and most will likely have ready access to training. However, incorporation of IFRS may present a unique challenge for smaller U.S. issuers to identify candidates willing to assume the financial expert position.
- In many ways the experience in the United States is likely to be similar to that of other jurisdictions that have adopted or are in the process of adopting IFRS. For example, Canada will be transitioning to IFRS beginning in 2011. The Toronto Stock Exchange requires each audit committee member to be financially literate or become financially literate within a reasonable period of time. The SEC should consider the experiences of Canada and other countries and incorporate such findings in its work plan.

As stated above, if the SEC mandates incorporation of IFRS into the U.S. financial reporting system, a sufficient transition or phase-in period will provide issuers with time to consider the implications incorporation of IFRS will have on their corporate governance processes in order to determine the appropriate course of action to address such issues by training existing members, or recruiting new members with IFRS expertise.

Securities Exchange Listing Requirements

The Commission questions whether incorporating IFRS into the U.S. financial reporting system would impact an issuer's ability to comply with quantitative securities exchange listing requirements. The CAQ is not aware of specific circumstances where this would be the case.

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We appreciate the opportunity to respond to the request for comment and would welcome the opportunity to discuss any questions you may have regarding any of our comments and recommendations.

Sincerely,

Cynthia M. Fornelli

Cindy Fornelli
Executive Director
Center for Audit Quality

cc: SEC
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