

STATEMENT OF GAYLEN R. HANSEN, NASBA DIRECTOR-AT LARGE
U.S. SECURITIES AND EXCHANGE COMMISSION
ROUNDTABLE ON INTERNATIONAL FINANCIAL REPORTING STANDARDS IN THE U.S.
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I would like to thank the Office of the Chief Accountant for the invitation to participate in this Roundtable.

As you are probably aware, accountancy regulation in the U.S. is separate and apart from professional associations, which is not the case in much of the world. In addition to the PCAOB, SEC and other Federal agencies, we have 55 State regulators. These State Boards are all members of the National Association of State Boards of Accountancy (NASBA), and collectively oversee the largest group of licensed accounting professionals in the world – over 650,000. State Boards of Accountancy are legislatively mandated, statutorily chartered and work closely with the profession to protect the Public Interest. So it is fitting NASBA, on behalf of our 55 State Board members, has been asked to address the key issues discussed here today. More about State Boards and NASBA is included in the Appendix posted online.

INTRODUCTION

To be clear, NASBA supports the concept of high quality global accounting standards. However, like the beauty pageant contestant hoping for “world peace and harmony”, support of a good idea is one thing, making it happen is quite another.

The case must be made that IFRS is not only a good idea, but is significantly better than what we already have. As regulators we have a responsibility to ask, “What is in it for us? What are the risks?” Considering the significant risks, the rewards must realistically offer superior and achievable benefits. Most importantly, we expect any change to clearly be in our National Interest.¹

To date, the case has NOT been made for IFRS. Accordingly, consistent with the observations in our 2009 Comment Letter on the 2008 Roadmap,² we believe the Staff should reconsider its 2010 Work Plan as well as its May 2011 “Condorsement” proposal.

I will elaborate, but will first note NASBA has nothing to sell, no fees, cost savings, credentials, books or CPE courses by which it would profit if IFRS is adopted. We are not vested in IFRS one way or the other. Careers at NASBA and State Boards are not dependent on IFRS going forward or being delayed. Our position is based solely on the National Interest.

So far we have witnessed considerable focus on the tactical “How and When” questions to get us to IFRS. Unfortunately, this passion ignores the gorilla in the room, the strategically more relevant

¹ PCAOB Board Member Charles D. Niemeier, September 10, 2008 speech to the New York Society of CPAS. http://pcaobus.org/News/Speech/Documents/09-10_Niemeier.pdf

² NASBA, February 19, 2009. File Number S7-27-08 “Roadmap For The Potential Use Of Financial Statements Prepared In Accordance With International Financial Reporting Standards By U.S. Issuers” <http://www.sec.gov/comments/s7-27-08/s72708-47.pdf>

question of “Why” we are even considering IFRS in the first place. While I cannot address all of our concerns in the time allotted, there are three broad areas worth reviewing.

DISCUSSION

1. The case has NOT been made that IFRS is better than U.S. GAAP. IFRS is the new kid on the block; consequently the burden of proof is on those advocating it. To this please refer to a study by Professor Donna Street and published in June 2011 by the Council of Institutional Investors.³ IFRS must stand on its own merits but the notion of one universal GAAP is largely a myth. There are actually numerous versions. It has been hyped that over 120 countries worldwide have adopted IFRS issued by the IASB. This is simply not true -- carve-outs resulting in jurisdictional versions are legion.

In reality, U.S. GAAP may be much closer to IFRS today than IFRS in many countries claiming adoption. I have spoken to Canadians who have indicated some of their companies are not doing anything other than wrapping the IFRS name around Canadian GAAP. The same has been previously reported about France. The crux of this may be that “high-quality” has yet to be defined in a context that is meaningful.

With an endorsement strategy, the SEC has come full circle from insisting on an IASB *as issued* version to now embrace a U.S.-flavored IFRS, with only a weak hope there will be few differences. There is no basis for such optimism considering the SEC has issued over 100 Staff Accounting Bulletins, a lengthy Financial Reporting Manual and its speakers regularly interpret GAAP at various conferences. These are required now by the SEC with a domestic private-sector standard setter. What will happen when a foreign de-facto standard setter is calling the shots is pure conjecture.

One may ask how many versions of GAAP do we need or even want.⁴ There is the plethora of IFRS carve-outs around the world already. The U.S. may go to one for large companies, perhaps another for smaller companies, the IASB version for Foreign Private Issuers, and potentially another for private reporting. Woe to the poor souls reconciling contracts or loan covenants requiring GAAP compliance. Like the Canadians and French, just because we may want to call IFRS “GAAP,” that doesn’t make it so. However, some legal clarity is needed to figure out whether some or all vintages of IFRS legally constitute “GAAP.”

GAAP could mean literally anything when the standards are moved around like a Rubik’s Cube. We have serious concerns the plan put forward to “condorse” IFRS will cause confusion and loss of investor confidence. This will happen whenever there is more than one version of whatever one calls GAAP.

³ Donna L. Street, University of Dayton, *Criteria for an Independent Accounting Standard Setter, How Does the IASB Rate?*, Council of Institutional Investors, June 2011.

<http://www.cii.org/UserFiles/file/June%202011%20White%20Paper%20-%20Int'l%20Accting%20Standards%20FINAL.pdf>

⁴ In a June 29, 2011 speech of SEC Commissioner Casey in Colorado Springs, Casey justifies a “two-GAAP” world by noting the Commission already permits foreign private issuers to use IFRS. This comment is disingenuous: the prior Cox SEC administration made the serious mistake of opening Pandora’s Box with its 2007 decision to accept IFRS from foreign private issuers. The mistake does not justify geometric compounding of the same error.

<http://www.sec.gov/news/speech/2011/spch062411klc.htm>

While admittedly, endorsement is better than outright replacement of GAAP, the original dream of comparability seems to have taken a back seat to the real agenda of some promoters – to get to IFRS at any cost and to pacify our friends abroad. Unfortunately, on this front, the U.S. overcommitted itself early on with various “Memoranda of Understanding” thereby subordinating the National Interest to a foggy notion of what may be perceived as a Global Interest. There is a major distinction. A Global Interest is not necessarily in our National Interest.⁵

When it comes to the driver of standards in this country, for too long we have looked primarily to the suppliers of financial reporting rather than the needs of users, especially investors. I have read the 200 plus comment letters sent to the SEC on the 2007 Roadmap. Despite the spin of overwhelming support for global standards, there is actually substantial concern and much outright opposition.⁶

I have *never* had a lender or investor request international standards. I have never even heard of such pleas. On the contrary, the call for IFRS always seems to be from the suppliers, primarily large multinationals and international accounting firms. It is often trumpeted that the G-20 is calling for IFRS. We submit that a couple of cryptic sentences in the 14th recommendation near the end of their pronouncement do not alone give any compelling reason why IFRS is critical to the world economy.

At this Roundtable there is not a single small issuer *without* international dealings. The group here today is not representative of the majority of small issuers. What is in IFRS for the small, purely domestic issuer – the mining company, restaurant chain or startup – and what are their concerns? Without resources to write comment letters, these folks are too busy just trying to survive. Before the SEC makes its final decision, it is critical we hear from those otherwise presumed to have nothing to say. This may mean more innovative outreach efforts are needed and appropriately filtered for bias.

Our system is significantly different than the rest of the world. We have different enforcement, educational, and licensing regimes. In our public markets there is a much higher level of personal investment and a performance emphasis. Our regulatory instincts are investor-focused. In many countries investors are secondary to business, which has a much greater say about standards. Stewardship is their main concern rather than performance. Abroad there is a hit and miss approach to regulation -- and very little approaching our SEC and State Board models. What little regulatory

⁵ *The Federalist Papers*, particularly Jay in No. 4 and Hamilton in No. 11. “But whatever may be our situation, whether firmly united under one national government, or split into a number of confederacies, certain it is, that foreign nations will know and view it exactly as it is; and they will act toward us accordingly. If they see that our national government is efficient and well administered, our trade prudently regulated, our militia properly organized and disciplined, our resources and finances discreetly managed, our credit re-established, our people free, contented, and united, they will be much more disposed to cultivate our friendship than provoke our resentment.” (Jay No. 4)

⁶ Tom Selling, *The Comments on the SEC Roadmap are Clear: Make a U-Turn*, The Accounting Onion, July 20, 2009, <http://accountingonion.typepad.com/theaccountingonion/2009/07/the-comments-on-the-sec-roadmap-are-clear-take-another-route.html>

oversight that does exist caters more to aid local businesses in the global marketplace.^{7 8} Thus, there are some fundamental structural distinctions that cannot be overcome simply with accounting standards. The regulator constituency is far different outside our borders. We should recognize this in any quest for comparability.

Finally, IFRS has been “sold” based on the unfounded hyperbole it is better because it is principles-based. This assertion is patently false. There are principles and rules in both U.S. GAAP and IFRS. Professor Lawrence Cunningham has written extensively about this sales pitch.⁹ There are indeed significant risks of over-emphasizing all things supposedly “principled.” Management has demonstrated repeatedly, when allowed free reign to exercise judgment, there will be increased pressure on detection risk and external auditors.¹⁰

2. Governance of the IASB must be fundamentally sound. The Staff has rightly identified this as a significant issue. Although the endorsement approach may bypass some legal concerns, even if the FASB becomes a proxy for the IASB, the result will be the same. The IASB *has* to be truly independent, financially¹¹ and politically. It must be transparent and responsive to its constituency. The Monitoring Board was established to answer these concerns. However, its infrequent meetings and composition of national regulators accountable solely to their own employers, do not constitute meaningful oversight. True independence of the IASB must be addressed before a serious adoption plan can be put forward.

National sovereignty in standard setting weighs heavily in protection of our National Interest. However, sovereignty must also be considered in light of States’ Rights. State Sovereignty extends to each of our 55 State jurisdictions as it relates to private reporting. The Roadmap and Work Plan correctly identify the impact of IFRS adoption on private reporting as an issue; however, little about this has been explored to date. Would the FASB remain as a robust standard-setter or would it be diluted to become a mere rubber stamp and go-between for the IASB?

⁷ This was widely reported in October 2008 when the IASB by-passed normal due process policies to rush to the aid of European banks. The outcome was not based on sound standard-setting procedure but solely in response to political pressure and appeasement of business interests. It was reported the IASB Chair threatened to resign but did not.

⁸ Another example is the transparency emphasis in the U.S. in recent years. By comparison, the IASB has had significant struggles convincing its constituency about the importance of accounting for derivatives and reporting of segment information.

⁹ *A Prescription to Retire the Rhetoric of “Principles-Based Systems” in Corporate Law, Securities Regulation, and Accounting*, Lawrence A. Cunningham, Vanderbilt Law Review, Vanderbilt University Law School, October 2007. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=970646

¹⁰ For example, under IFRS there is considerable leeway for management to choose when and how to write-up assets and capitalization of intangibles and research and development expenses.

¹¹ See on page 13 from above *Criteria for an Independent Accounting Standard Setter*, noting that the 2011 IASB budget plans on less than half of its funding from publicly sponsored/nationally administered financing, 26% from accounting firms and 8% direct voluntary contributions. By contrast the FASB is now substantially financed as a result of the accounting support fees under the Sarbanes-Oxley Act.

It is clear an IFRS model in the U.S. will be a baseline for private financial reporting by private companies constituting a critical source of job creation, employment and GNP. We repeat that States do have sovereignty in this area and this fact is clearly acknowledged in the Sarbanes-Oxley Act.¹²

Also from a sovereignty standpoint, it would be helpful if those regulators vested with a voice in private reporting be included in the SEC's ongoing discussion agenda. This would be consistent with and responsive to the ACAP recommendations.¹³

3. Costs need careful consideration and must be reasonable. While this has been identified as a concern by the Staff, very little has been done to actually address the issue. Some believe the cost will be staggering and easily exceed by several magnitudes the costs of adopting Section 404 of Sarbanes-Oxley.¹⁴ What is the cost likely to be and who is going to bear the burden? While conversion costs of the largest issuers may be offset by benefits accruing directly to them, by comparison from a percentage standpoint, the cost will be incredibly greater to the small issuer with virtually no benefit.¹⁵

Ironically, at a time when the country is struggling financially, to place this additional burden on the backs of small business is unreasonable and certainly not equitable. Further, the cost of training will be pervasive and extend to all sectors of the financial reporting community, including users, regulators, academia, and the public at large.

As it relates to the accounting profession, the IFRS proposal heavily favors the largest auditing firms at the expense of small practices. There has been a long and storied history of concentration within the profession and a lack of competition. This has been exacerbated in recent years and has been the subject of significant national and even international concern.¹⁶ Essentially, going to multiple versions of GAAP will create a community of CPA firm "haves and have not's." Small firms simply do not have the resources to support multiple versions of GAAP. This is not healthy for the nation, nor the profession, and certainly not for the investors.

¹² *Sarbanes-Oxley Act of 2002*, Section 209, also mentioned in Sections 104 and 105.

¹³ We note a recommendation in the 2008 U.S. Treasury Department's *Advisory Committee on the Accounting Profession* (ACAP), to "require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes." To date such meetings have not occurred. <http://www.treasury.gov/press-center/press-releases/Pages/hp1158.aspx>

¹⁴ For example see comment letter dated January 28, 2009, to the SEC from James F. Barlow, Senior Vice President, Corporate Controller, (Principal Accounting Officer), Allergan, Inc. <http://www.sec.gov/comments/s7-27-08/s72708-25.pdf>

¹⁵ The only substantive benefit for small domestic issuers is a lower cost of capital. However, given that the U.S. already has the lowest cost of capital in the world (argued by Niemeier in his speech noted above), how does IFRS improve an incentive that is already satisfied by U.S. GAAP?

¹⁶ For example, the 2008 ACAP hearings identified concentration and competition as a serious threat. In a similar vein, in late 2010, the European Commission issued a Green Paper on the topic and is now exploring the same issues. http://ec.europa.eu/internal_market/auditing/docs/liability/700996_en.pdf

CONCLUSION

International standards may be likened to the Holy Grail, worth searching for but only if you think there is a reasonable chance of finding it. In the meantime, there is a real risk of obsessing in the quest at the expense of more pressing and worthy goals. There are extremely high risks in the “condorsement” approach suggested by the Staff. We may not know for several decades whether it was a very bad idea and, if so, in time to recover.

We strongly support continuation of the FASB as constituted in its present form. With regard to embracing IFRS, this is best undertaken through convergence when appropriate, subject to legal due process, but only based on a consistent and logical theoretical foundation. Convergence simply for the sake of convergence is not a good idea. Further, convergence based on compromise represents acceptance of mediocrity, inconsistent with any claim to high-quality standards.

The FASB should not become a mere conduit to import IASB standards. We understand the endorsement approach is being considered as a matter of convenience because the SEC cannot concede or delegate its oversight role. However, endorsement will not lead to comparability nor high quality standards, but instead carve-outs and cut-ins. We fear endorsement will be tantamount to surrender of investor protection. Once such an arrangement is set in motion, it will be nearly impossible to reverse.

Any arrangement involving the IASB should not be considered until all U.S. stakeholders are satisfied with IASB independence and governance. Further, the cost of embracing IFRS should be thoroughly vetted before any further commitments to the IASB are made or even implied. In all instances both National and State Sovereignty must be respected.

A beauty contestant’s naïve quest for a world of peace and harmony is understandable, even admirable. However, weakening oversight of our own standards is neither, and is clearly not in our National Interest. Why we would impose this upon ourselves, without compulsion, is even more remarkable.

We recognize the current debate was not the making of the current Commission or Staff. You are to be commended for giving the project your good faith efforts. Again we ask you to reconsider the current proposal on the table. It is time to move on to more pressing matters.

Respectively submitted,



NASBA Director at-Large

I. STATE REGULATION OF ACCOUNTANCY IN THE U.S.

The U.S. Constitution reserves professional licensing to the States.

The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved for the States respectively, or to the people. – Amendment X

With this authority in our Bill of Rights, States have empowered its Boards of Accountancy with sole authority to establish licensing requirements for all Certified Public Accountants. State licensure is required by all independent accountants and auditing firms seeking to practice before the SEC and other Federal agencies.

- Federal laws recognize this Constitutional authority. For example the Sarbanes-Oxley Act acknowledges State regulatory authority over the audits of nonissuers.

In supervising nonregistered public accounting firms and their associated persons, appropriate State regulatory authorities should make an independent determination of the proper standards applicable, particularly taking into consideration the size and nature of the business of the accounting firms they supervise and the size and nature of the business of the clients of those firms. The standards applied by the Board under this Act should not be presumed to be applicable for purposes of this section for small and medium sized nonregistered public accounting firms. – Section 209

- Consistent with Federal and State laws, State Boards regulate all CPAs serving issuers and nonissuers, whether they are auditors in public practice or in private practice as officials of reporting entities. Foreign auditors must also be licensed within the states where they perform work.
- State Boards are empowered to establish accounting, auditing, independence, ethics and continuing practice standards for all CPAs and CPA firms engaged in financial reporting of nonissuers. *Although not required to do so*, State Boards have historically *looked to private-sector standard setters* to fulfill those requirements. Such private-sector standard setters currently include the FASB and the AICPA's auditing and ethics standards boards. This approach to standards parallels that used by the SEC.
- State Boards enforce standards and discipline CPAs and their registered firms for violations of SEC, PCAOB, GAO, DOL and other Federal and State agencies' standards, as well as their own separate and distinct State accountancy regulations. Disciplinary actions range from fines, reprimands, additional education, pre or post issuance report reviews, and practice restrictions all the way to suspension or revocation of licensure. These disciplinary remedies have the

practical impact of State Boards serving as a gatekeeper for CPAs and CPA firms seeking to practice before the SEC and other Federal agencies.

- State Boards are solely responsible for establishing requirements of moral character, formal academic education, minimum experience and examination for licensure as a CPA. They also set standards for mandatory continuing education and quality reviews of auditing firms. In addition, State Boards have certain responsibilities under Sections 104 and 105 of the Sarbanes-Oxley Act in the inspection, monitoring, investigation and discipline of CPAs and auditing firms registered with the PCAOB.
- State Boards are composed of over 400 members of whom more than 100 are non-CPAs (“public members”). They are drawn from public and private practice, government, not-for-profit organizations, law and academia. Most are appointed by State governors and are highly accomplished individuals in their own right. Appointments are typically subject to specific term limits. None of the appointees are separately compensated for their voluntary service and they and their employers donate their substantial professional time. The focus of State Board members is solely on public service, including protection of investors.

II. NATIONAL ASSOCIATION OF STATE BOARDS OF ACCOUNTANCY

All 55 Boards of Accountancy constitute the membership of the National Association of State Boards of Accountancy, and respectively, regulate over 650,000 CPAs and 47,000 public accounting firms. As such, NASBA represents the largest collective body of accounting regulators worldwide.

- NASBA’s mission is to enhance the effectiveness of its Boards by serving as a coordinator and forum for the Boards, allowing for exchange of views, and providing research and overall regulatory guidance.
- Founded in 1908 to aid States in developing uniform licensing procedures, NASBA has evolved into a broad-based organization dealing with all aspects of State regulation of CPAs and their firms.
- NASBA serves as the voice of State Boards in relationships with national and State regulators, Federal agencies, the U.S. Congress, professional organizations and the news media.
- NASBA is led by a full-time CEO, David Costello, who is supported by approximately 210 professional and administrative staff, and a volunteer Chair elected by the member State Boards. The NASBA Board of Directors is composed of 20 State Board representatives.
- Since passage of the Sarbanes-Oxley Act and formation of the PCAOB, NASBA’s activities with the PCAOB and SEC on behalf of the 55 State Boards have increased significantly.

- Many of NASBA's activities are directed toward cooperative coordination of Federal, State and foreign regulatory systems, U.S. and international professional practice standards, practice monitoring, discipline and mobility. NASBA is represented on the PCAOB's Standing Advisory Group, the AICPA's Auditing Standards Board, Board of Examiners, Professional Ethics Executive Committee, Peer Review Board, and the International Federation of Accountants (IFAC) Consultative Advisory Groups of its auditing, ethics and education boards.

- NASBA was represented on the U.S. Treasury Department's *Advisory Committee on the Auditing Profession*, and more recently the FAF/AICPA/NASBA *Blue Ribbon Panel of the Financial Accounting Foundation* to consider the development and promulgation of accounting standards for private entities.