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Securities and Exchange Commission
100 F Street, NE
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Re.: Comment on Acceptance From Private Issuers of Financial Statements Prepared in Accordance With International Financial Reporting Standards Without Reconciliation to U.S. GAAP (Release No. 33-8818; July 2, 2007 / File No. S7-13-07)

Chairman Cox and Commissioners,

Your request for comment is timely and appropriate. Most knowledgeable parties would probably agree that uniform international accounting standards would be a good thing; it would be great if all financial statements had a common baseline and were therefore comparable. Although conceded as a worthy goal, the underlying ramifications of replacing U.S. generally accepted accounting principles (GAAP) with International Financial Reporting Standards (IFRS) are beyond significant and require careful analysis. The Commission has requested comment on the reconciliation requirement of foreign private issuers. On July 25th it also asked for input on extending the use of IFRS to domestic issuers. The comments below address neither foreign nor domestic reporting specifically, but rather, focus on a more fundamental topic: "Who should be establishing U.S. accounting standards for our capital markets?"

The core concern is the underpinnings of the international standard-setting structure and its relative lack of independence vis-à-vis the Financial Accounting Standards Board (FASB). The observations below are relevant to the Commission's publicly stated goals that Release No. 33-8818 implicitly re-articulates.

The International Accounting Standards Board (IASB) is a private sector creation, meaning that it answers primarily to a non-regulatory constituency. That constituency includes much closer ties to accounting membership trade associations, international accounting firms, and large corporate, institutional and governmental organizations than does its FASB counterpart. These alliances are manifest in IASB participation and funding, which raises questions about its actual independence.

In the shadows of the Enron and WorldCom collapses, passage of the Sarbanes-Oxley Act (SOX) by Congress in 2002 was a cornerstone event enhancing independence of both accounting firms and also the private sector standard-setters that the SEC looks to for leadership within the accounting profession. Given the long and well documented history that ultimately led to an independently financed FASB, it is remarkable that the Commission would so quickly conclude that shifting this critical role to a foreign-controlled body is in our national interest without public analysis and discussion of the pros and cons. Such a dialogue should be unfettered by one-off questions – e.g. "Should the IFRS to U.S. GAAP reconciliation be discontinued?" or, "Should domestic issuers have the option of electing IFRS versus U.S. GAAP?" Those questions have leap-frogged a more relevant question: "Does the IASB stand up to public scrutiny particularly when it may be subject to external pressures from its funding sources?"

The subtle focus on peripheral issues is particularly troubling since the SEC is solemnly charged by Congress with the final responsibility to establish national accounting principles and practices.[1]

Before making its decision, the Commissioners should consider the following:

- While both the FASB and IASB are "private sector standard-setters," the FASB is subject to direct governmental oversight by the SEC. There is no such regulatory safeguard with the IASB – it is an organization of its own making and does not have statutory roots nor independent public oversight;
- With the advent of SOX, the FASB is now 100% financed by the accounting support fees paid by public companies. The IASB does not have a similar funding mechanism and is substantially dependent on major audit firm and large corporate contributions (its 2005 budgeted receipts from these two sources was 61%[2]). This strongly suggests that the FASB enjoys significantly greater financial autonomy thereby enhancing independence, than does the IASB;
- With a third of the IASB represented by current or retired Big Four partners, Big Four accounting firm participation is much deeper than at the FASB.[3] Three of the Big Four firms have IASB representation (a total of 33% of the voting total), and KPMG by itself, with 3 of the IASB's 15 members controls 20% of its vote.[4]
- Significantly, FASB members must relinquish <u>all</u> ties to prior employers. This is apparently not an IASB requirement;[5]
- The IASB is subject to intensive geopolitical pressures. For example, the European Commission requires that IASB standards be approved by their legislative process before they become effective in the EU. This approach is not uncommon in internationally and adds pressure to an IASB seeking acceptance of its standards. The point is: for the U.S., adopting IFRS would be tantamount to handing foreign parliaments a significant political role in our standard-setting process. By contrast, the U.S. Congress historically has taken a "hands-off" approach, astutely recognizing the hazards of injecting politics into the complex mix of standard–setting;
- The idea of one universal IFRS is largely a myth. There are actually numerous versions of nationally recognized IFRS: there is an Australian IFRS, Hong Kong IFRS, etc., an actual potpourri of standards. While the IASB is attempting to reverse this little-discussed situation and elevate its own brand, it is a misleading at

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[1] See, e.g., Securities Act of 1933, 15 U.S.C. §§ 77g, 77s(a), 77aa(25) and (26).
[2] http://www.iasb.org/About+Us/About+the+Foundation/Future+Funding.htm . The IASB's audited financial statements do not disclose any details about significant contributors.
[3] IASB current or former Big Four partners include: KPMG – Gélard, O'Malley, Tweedie; D&T – Smith; PWC – Yamada.
[4] KPMG was formed in 1987 with the merger of Peat Marwick International (PMI) and Klynveld Main Goerdeler (KMG) and their individual member firms. Given KPMG's deep European roots, it is hardly surprising that it has greater IASB influence which many regard as being dominated by European interests.
[5] Two of the 15 IASB members are part-time: John T. Smith (Deloitte) and Mary E. Barth (Stanford University).

this point to assume that other sovereign nations have or will abdicate their national interest to a body over which they have no control. Why then should we?; and,

- Standard-setting is an expensive proposition necessitating retention of the best and brightest. However, it appears that the IASB is far more costly than the FASB with over twice the number of board members and compensation levels 50% higher. In 2006, the IASB paid its chair and board members $893,000 and $725,000, respectively.[6] By contrast, in 2005 the FASB chair and board members were paid $595,000 and $484,000.[7] Even with the one year difference (FASB's latest publicly available data is for 2005), the IASB is far more expensive to run than the FASB.

Aside from autonomy and structural concerns, there is also the practical aspect of IFRS implementation. It is highly likely that if the SEC were to agree to adopt IASB standards that U.S. practitioners would need significantly more time to become get up to speed on IFRS. For instance, consider the following:

- Generally speaking, the accounting curricula of U.S. universities is not focused at all on IFRS;
- The Uniform CPA Examination currently does not test for IFRS proficiency and the earliest this could conceivably occur would be 2009 or 2010, ***even if universities immediately began covering the subject matter today;***
- Accounting practitioners, both public and private, are largely unfamiliar with IFRS; and,
- Current IFRS continuing education offerings for practitioners are in the earliest stages of development.

There may be a subconscious tendency to regard IFRS as an easy fix for the many shortcomings of U.S. GAAP. A more realistic expectation would be that the IASB may only solve a few of those problems in exchange for accepting other risks. Even if the structural and practical problems noted above are satisfactorily addressed, there are a myriad of others, such as the impact of reconciling IASB standards to the U.S. federal income tax system. Also, there are serious differences and gaps between U.S. GAAP and IFRS – e.g. accounting for leases, derivatives, insurance and income taxes. U.S. GAAP has been discussed, debated and interpreted for decades and has stood the test of time. By contrast, for all practical purposes – IFRS financial statements have only been issued in any large number for the past three years.

It might be instructive to consider the evolution of U.S. GAAP in light of your proposals. U.S. GAAP evolved in an environment that 1) has a unique legal system, and 2) incorporated much broader capital markets with wide-spread individual participation than what is found in the rest of the world. U.S. GAAP was developed inside of a legal framework designed to protect those investors – and a rules based system grew in response to that environment. Our system therefore is couched in shareholder protection. For sure, other countries are catching up with us. When they eventually do catch up, it could be reasonably argued that they too will have more litigious societies and stronger investor safeguards. In that circumstance, one of the touted advantages of international standards – a principles based

[6] From IASCF's 2006 Annual Report pp. 32-33 and converted at a July 31, 2007 USD/GBP .4920 exchange rate.
[7] Based on Schedule 10 of FASB's 2005 Form 990, *Return of Organization Exempt from Income Tax.*

framework, will likely have also evolved into a more rules based system, dissipating the perceived original intent of a principles-based orientation.

Another distinctive aspect of our financial markets is that its capital freely flows in two directions – private investment frequently becomes public equity and vice-versa. Private hedge funds and private equity funds are prime examples of the flexibility and liquidity of this phenomenon. Therefore in the U.S., accounting standards are just as important in the private sector as they are in the public realm. While the arguments for "Big-GAAP / Little GAAP" and "Private GAAP / Public GAAP" have been debated for decades, for the most part our system accommodates a single set of rules. While there are justifiable differences that U.S. standard-setters have and will take into consideration in special situations, the larger picture is that GAAP is GAAP is GAAP. Adopting a new model with multiple standards would erode and negate the fundamental advantage of having a single bedrock upon which all financial reporting rests.

The SEC's jurisdiction extends to publicly traded securities and the companies that issue them. However, the ultimate outcome of replacing the FASB would have a "trickle down" effect on private company standards which fall under the jurisdiction of state boards of accountancy.[8] If U.S. GAAP and by extension the FASB is replaced, that trickle could turn into a monsoon for non-public entities.[9] This singular contingency should not be ignored.

There are fundamental public policy decisions that transcend the current populist IASB bandwagon. Please slow down long enough to adequately publicly examine and resolve those issues before making your decision.

Thank you for your consideration, [10]

[8] *U.S. Constitution*, Article 10.

[9] The implication being that if the SEC were to replace the FASB, the private sector would still need to finance a standard-setting mechanism. The SOX accounting support fees that finance the FASB could conceivably end up subsidizing the IASB leaving private companies with nowhere to turn for technical guidance.

[10] *I have been engaged in SEC auditing and financial reporting my entire career, a period exceeding 30 years. I am employed as an audit partner with the Colorado accounting firm of Ehrhardt Keefe Steiner & Hottman PC. I am also a member of the Colorado State Board of Accountancy, the National Association of State Boards of Accountancy (NASBA), the AICPA's Professional Ethics Executive Committee (PEEC) and the PCAOB's Standing Advisory Group (SAG). I hold an MBA in International Business from Cal State Fullerton. However, the views expressed herein are my own and should not be regarded as an official position of any of the foregoing bodies.*