David Tweedie

Profile: Sir David Tweedie

It’s Not Rocket Science: Views on Why the Accounting Profession Should Pursue Simplicity in Standard Setting

The chairman of the International Accounting Standards Board addresses the challenge of simplifying financial accounting and tells us what needs to be done to make financial reports more understandable to the average investor.

Intro

Financial reporting standard setters are often blamed for making financial reports complex and bulky. In this interview, David Tweedie, the outgoing chairman of the International Accounting Standards Board (IASB), endorses the need to simplify and condense financial reports, but he denies that the fault can be assigned to standard setters alone. He says that simplification is the responsibility of everyone involved: not only standard setters, but also preparers of financial accounts, board members, accountants, and auditors. In this interview, Sir David points out who could do what in order to make financial reports more understandable to the average investor. In his own words, “We do need to measure these things, we just don’t need to do so in such a complicated way!”

David Tweedie: A brief bio

Sir David Tweedie was educated at Edinburgh University (BCom 1966, PhD 1969) and qualified as a Scottish Chartered Accountant. He was appointed technical director of the Institute of Chartered Accountants of Scotland in 1978. From there, he became national technical partner of the then Thomson McLintock & Co in 1982. In 1987, his firm merged with Peat Marwick Mitchell & Co and he was appointed national technical partner of KPMG Peat Marwick McLintock. In 1990, he was appointed the first full-time chairman of the (then) newly created Accounting Standards Board, the committee charged with the responsibility for producing the UK's accounting standards. Since 2001, he has served as the chairman of the International Accounting Standards Board (IASB). He is a visiting professor of accounting in the Management School at Edinburgh University.

He has been awarded honorary degrees by eight British universities, the ICAEW's Founding Societies Centenary Award for 1997, and the CIMA Award 1998 for services to the accounting profession.

See also “About the International Accounting Standards Board” below.

About the International Accounting Standards Board (IASB)

The IASB is the independent standard-setting body of the International Financial Reporting Standards (IFRS) Foundation. Its 15 full-time members are responsible for the development and publication of IFRSs, including the IFRS for SMEs, and for approving Interpretations of IFRSs as developed by the IFRS Interpretations Committee.

All meetings of the IASB are held in public and webcast. In fulfilling its standard-setting duties, the IASB follows a thorough, open, and transparent due process of which the publication of consultative documents, such as discussion papers and exposure drafts, for public comment is an important component. The IASB engages closely with stakeholders around the world, including investors, analysts, regulators, business leaders, accounting standard setters, and the accountancy profession.

- From www.ifrs.org

About the International Financial Reporting Standards (IFRSs)

The International Financial Reporting Standards (IFRSs) set out recognition, measurement, presentation, and disclosure requirements dealing with transactions and events that are important in general purpose financial statements. IFRSs are based on a conceptual framework, which addresses the concepts underlying the information presented in general purpose financial statements. The objective of the framework is to facilitate the consistent and logical formulation of IFRSs. It also provides a basis for the use of judgment in resolving accounting issues.

IFRSs are designed to apply to the general purpose financial statements and other financial reporting of all profit-oriented entities. Although IFRSs are not designed to apply to not-for-profit activities in the private sector, public sector or government, entities with such activities may find them appropriate. The International Public Sector Accounting Standards Board (IPSASB) prepares accounting standards based on IFRSs for governments and other public sector entities.

IFRSs apply to all general purpose financial statements. Such financial statements are directed towards the common information needs of a wide range of users, for example, shareholders, creditors, employees, and the public at large. The objective of financial statements is to provide these users with information about the financial position, performance, and cash flows of an entity to assist them in making economic decisions.

- From www.ifrs.org/IFRSs

Financial reports should be simplified and condensed

How could we make financial reporting more useful?

“One of the things we tried in the UK was to simplify the accounts for private investors. The problem is that companies have become more complex, and in turn, so have their financial reports. This makes it difficult for the average private investor to interpret these complex statements, and now they need more help. I wrote a book with Tom Lee, about 30 years ago now. In doing research to write the book, we discovered that at the time, the only people who truly understood the accounts were accountants. Part of the problem is the use of accounting terminology such as *reserves*, which respondents understood as cash reserved for a rainy day. They didn’t understand why there was cash on one side of the balance sheet and reserves on the other. Neither did they understand the term *current assets*, which they thought meant all the assets you have at the present time. The lesson was that we accountants needed to better define our terminology for non-accountants.

“More recently, we tried to find out what exactly we should include in the accounts if we simplified them. We wanted to try to reduce the number of disclosures. When we told the analysts that we were going to take out one-third of the disclosures, and asked which third they would want to go, we got nowhere. They told us they needed everything. So, if we are going to fix this thing, we should start with the interim reports and then say, 'Right, we are going to start again. Here are the interims. Now, let's build them up. What exactly is essential?' Because if stakeholders manage with these interim reports for three quarters of the year, now, how come the annual reports need to be so absolutely colossal? And does all this information really help them, or is there stuff we can dump in a computer file, which they can access online if they wish? We have got to shrink the accounts, and there are lots of ways we can actually do this (see also 'The postman can only carry two annual reports'). At present, the Institute of Chartered Accountants of Scotland and others are undertaking a study on behalf of the IASB. The study examines each of our standards to determine whether we can remove the present disclosure requirements and replace them with principle-based disclosure objectives, leaving it to the companies themselves to determine how to meet those objectives."

The postman can only carry two annual reports

"In a public statement, a UK group finance director once said that the postman can only carry two of his annual reports. Standard setters got the brunt of the criticism, however, when I went through the company's annual report, the bulk of it was legal disclosures and US reporting requirements, and I thought to myself, 'This has not got anything to do with us, the standard setters.' You are covering yourself, and you want one document out for all the markets, while you could have different documents for different markets."

No complete overhaul of legacy accounting standards

Wouldn't simplified financial reporting also benefit from simplified financial reporting standards?

"When I finish this job as IASB chair in a few months time, I will feel slightly frustrated because we didn't do what we originally intended to do. When we started 10 years ago, we inherited a set of accounting standards that had been developed by a part-time board over the previous 20 years. They were OK, but the International Organization of Securities Commission (IOSCO) felt that they were not suitable for use by major financial markets. We spent the first three or four years cutting out the bad bits and putting other bits in, but with Europe's 2002 decision to adopt IFRSs from 2005, we just didn't have the time to do a complete overhaul. More and more countries were deciding to adopt the standards, so we had to bring them up to scratch as quickly as we could.

"Looking at the current financial reporting standards, I think there are three standards that are horrifically complicated: IFRS 2, which addresses shares-based payment, financial instruments (IAS 39), and income taxes (IAS 12). All three of these were originally US standards. I don't want to be accused of being anti-American, which I am not, but there was a big US influence on the old IASC,[1] as far as the standards for financial instruments and income taxes were concerned. And the share-based payment

[1] International Accounting Standards Committee, the predecessor of the IASB

standard was put in because it was the quickest way to stop the crisis around share-option remuneration spreading across the world.

"We also need to sweep all the smoothing mechanisms out of accounting, such as the one for pensions. Suppose you have a pension fund of 40 million assets and 40 million liabilities and the assets have fallen by 10, then you have a deficit of 10. Yet under standard FAS 87 of the US Financial Accounting Standards Board (FASB), which the IASB incorporated, companies could say, 'Well, some of that deficit is just noise and is measured at 10% of assets or liabilities, whichever is highest. In this case, liabilities are higher with 40 million, so 10% is 4 million. They then knock a million off the 10-million deficit, so they are now down at 6 million. And, as pensions are long term, they spread that deficit over the working lives of the employees, which is, say, 10 years. So instead of 10 million, companies are only showing a deficit of 600 thousand. And as I often say: 'Explain that now to your grandmother!' You may as well take the 10 million, divide that by the number of miles to the moon, and multiply that by your shoe size, and you are showing 600 thousand. And it doesn't mean a thing. You have a deficit of 10 million. Stop messing about it. Just show it!"

My grandmother would sleep better though…

"But that is not the point. Look at the major US motor companies with all of their employee pensions and health insurance policies. These commitments brought the US motor industry to its knees. They treated them on a 'pay as you go' system and did not seem to understand what they had signed up for, until the FASB made them account for it. As a result, when they actually had to report it to their shareholders, the companies were almost worthless. That is lousy accounting! So people who say that accounting shouldn't change behavior are absolutely wrong. If management had had to report the commitments that they were making to their shareholders, they might not have signed off on all these agreements, and they might still be a going concern instead of needing life support systems to stay in business."

Composition of the IASB getting more diverse

Isn't the IASB made up of too many technicians for it to perform such a simplification overhaul?

"When the IASB was formed, that may have been true. It had to be able to match the FASB for technical know-how. As a result, the initial Board was populated with financial reporting experts and career standard setters, which is what we needed at the time to get up and running. However, if you look at the composition of the Board over the last three or four years, that has been changing. The new crop of Board members have practical experience in the use, preparation or regulation of financial statements. In the last two to three years, the Board has been joined by three analysts, two former CFOs, two former regulators, and a number of former auditors. So the Board is getting a more and more diverse base. You still need the technicians in the sense that you need people who can ensure that the drafting of the standards is sufficiently robust, but the Board also has a lot of people who can say, 'That doesn't make sense,' and have the power to veto it."

IASB will tackle complexity in accounting standards

What could the IASB do reasonably quickly to make accounting standards less complex and difficult?

“As I hinted earlier in the interview, the complexity of IAS 39 (Financial Instruments) had been causing problems. We have been trying to change that standard for a long time, but actually the financial crisis gave us an excuse to accelerate the project, and we are close to completing this work.

“We have the other standards I mentioned (Income Taxes and Shares-Based Payment) on our agenda to start after 2011. Knowing that, I have been in touch with the national standard setters, and they have set up a group that meets twice a year. I encouraged them to pull apart these two standards and come back with much simpler proposals. Now, the UK is leading the one on income taxes and the French are leading the one on shares-based payment. Both groups are making good progress. The IASB will shortly begin a consultation on the future agenda of the Board once all of the convergence projects are completed, but as a result of the groundwork carried out by these national standard setters, the homework will be done by then and that will accelerate the simplification of these standards.

“We have started to speed projects up this way because, if we could start from scratch, we would spend a couple of years working out all the various options, the pros and the cons, and which options might be the best ones. That will now all be done for us by the various national standard setters. So we, the Board, will pick the projects up at the discussion paper stage, which includes the pros, cons, recommendations, and key considerations. That saves us two years, allowing us to move straight on to drafting standards once we get the comments on the discussion paper back. So, we try to make this a partnership and bring everybody in.”

Bottom-up versus top-down development of standards

Can you explain the fundamental differences between the IASB and its US counterpart the FASB?

“The IASB operates in a different way from the US FASB. The FASB traditionally uses a bottom-up approach, asking, ‘What are all the issues that may arise in practice?’ Then, the FASB builds the standard based on all the potential situations that may arise. Whereas, I think those of us who have been trained in the UK or elsewhere with a principle-based approach, use a top-down approach. They more or less ask, ‘What is the answer in broad terms?’ And then, ‘How much guidance do we have to provide to get there?’ Now you end up with a totally different style of standard. And the real questions then are:

- Do we really want to be principle-based?
- Do we want to firmly put the responsibility for financial reporting in the hands of directors and auditors?

“Dealing with all the possible specific scenarios greatly increases the length of a standard. The standard setter’s approach is, ‘I can deal with 80% of the problems in probably 20 to 30 pages, but if I have to cover 95% of the issues, then it is going to be 100 or 300 pages.’”

Accounting profession should resist urge for additional rules, exceptions, and guidance

How can we limit the explosion of rules and interpretations to explain the principles?

"As I often say, 'We get the standards that we deserve.' The new standards developed by the IASB (standards with an IFRS prefix, as opposed to an IAS prefix, which were inherited from the old IASC) are principle-based standards, the best of which are short and sharp. But already we hear, 'Can we have an exception here? Can we have that? What do I do in this situation?' And here we go. People are asking for rules, and exceptions from rules, and guidance for rules.

"So the accounting profession really has a big choice to make, and I think that if it doesn't make the right choice, it is doomed to becoming little more than a profession of box-tickers. The search-engine profession.

"So we are now in a situation in which principles have really been embraced, and we want to give minimal guidance so that people can implement the standard, and no more. The IFRS Interpretations Committee only issued three interpretations (IFRICs) on IFRS standards last year for the whole world, while the US issued many times more for the US alone, and we must not go that way. So I really think this is a case where the accounting profession must have the confidence to stand up and say 'This doesn't make sense,' and they must stop saying, 'Could you please insert an extra rule?'

"It is especially the auditors who ask for additional rules so they can say to their client, 'You can't do this.' Auditors must have the guts to tell their client that something is wrong or should be done differently and not ask for an extra rule to validate their assertion.

> *"If you pick up those financial accounts and look at them, would they really tell what you, as its external auditor, know about that company? If they don't, you got it wrong!"*

"Now, we are pushing back on giving auditors interpretations of the accounting standards. I can't remember how many requests for interpretations we turned down last year, but probably in the region of 30 to 40. These requests came all from the accounting firms asking, 'Can you deal with this point?' Now, why do they constantly have to ask? The fact is that they have to make the judgment themselves because we are refusing to answer and that is gradually seeping in. So it is education that needs to happen (see also 'Development of professional judgment, that's what it is all about')."

Development of professional judgment, that's what it is all about

"It was interesting that when Europe switched to IFRS, we thought we would have an avalanche of requests for interpretations, but we didn't. The technical partners of the firms did their jobs and kept them back, and the firms settled any interpretation questions with their clients. And that is very important, the development of professional judgment within the profession. Do you want a rulebook or to be able to look at the substance of the transaction and act upon it?

"Here you also come against integrity. Do we need to be told what to do when faced with moral dilemmas and things like that? I think accountants need to go right back to the basic questions:

- *Who is your client?* Your client isn’t the guy in that smart suit across the desk. It is the shareholders of the company, as well as the broader financial community outside there. That is whom you are working for.
- *What is this scheme all about?* We often say: ‘If you pick up those financial accounts and look at them, would they *really* tell what you, as its external auditor, know about that company?’ If they don’t, you got it wrong!”

Also non-executive directors need to stand up against unacceptable accounting

What is the role of company boards in relation to financial accounting?

“Investors should feel confident that the directors are in control. We need the non-executive directors to stand up against what I would consider to be unacceptable accounting. Good corporate governance is therefore critical. How do you appoint non-executive directors? That is a key question (see also ‘The type of board member we need’).”

The type of board member we need

“One of the salutary experiences of my professional life because it reaffirmed my faith in the accounting profession was visiting one of my major clients where we had had a terrible job with the audit: if you would say the acceptability of its profit would be, let’s say, somewhere between 95 and 100 million, the client was at 130 million. And it took us several weeks hauling the client back with acrimonious discussions until we got it just within 100 million. And the first question I was asked by the chairman of one of the FTSE 100 companies who was a non-executive board member in this company was: ‘Where do this company’s accounting policies fit between very acceptable and totally unacceptable?’ And I told him just within acceptable. And he asked if I could leave the room. Apparently, what happened was that he and three other chairmen of FTSE companies told the chairman of this company’s board that the finance director should be fired or should resign that day. And they fired the finance director. And the next year everything was fine. That was corporate governance!

“These guys obviously didn’t want their reputations tarnished by some upstart finance director who was playing games with the accounting. Now we need that sort of person on boards.”

Principles are easier to defend than rules

Isn’t it very difficult to go back to principles and professional judgment without tackling litigation?

“You should actually fear litigation more in a rules-based environment than in a principle-based environment. I am referring now to an Institute of Chartered Accountants of Scotland conference in New York in which one of the presenters, Michael Young, held up a copy of the US Constitution saying, ‘You can defend your actions vis-à-vis a principle, such as those in the US Constitution, but if you ignored something on page 743 of a rules-based standard, then you are finished!’ And that is it.

"If you want to have a search engine for the accounting profession you stick to the rules. But if you want to actually practice accounting and apply professional judgment, you better use principles."

Accounting firms should only plead guilty to genuine negligence

What do you think the barriers are to principle-based accounting?

"I think the accounting firms have part of the answer in their own hands. We have to get them to defend the use of principle-based accounting. They must make sure they only plead guilty to charges of genuine negligence (see also 'That's not negligence').

That's not negligence

"One of the things that I was asked was, 'What happens if you meet an accounting issue that you have never met before?' Well, there is a standard procedure for that.

"Suppose you are the audit partner. You would have to chat with your technical partner, who would then chat with others who had clients in the same industry. They would probably pull in a senior partner or two, discuss it with the technical partners of some of the other firms, and come up with what they believe the answer should be. You would also look through all the standards and literature you could find. If you document all this, there is nothing more you can do. You might make the wrong call, but that can happen, and that is not negligence. That is the way you have to handle this."

"When you look at the UK, we don't have that many lawsuits against audit firms. Even under the old accounting standards, we didn't have that many. And Australia is the same. You have the odd disaster like Polly Peck, but the problems are not often caused by a misjudgment or an accounting standard. It has been lousy auditing and/or caving in to senior executives that has caused problems. So I haven't seen many litigation cases in which someone really made a wrong judgment based on a principle and a standard. Oftentimes, the standard is pretty clear, but the company has chosen not to apply it. That is part of the issue because if you look at some of the cases in the US, even Enron, while prosecutors said it was an accounting disaster, it was actually management breaking the rules, and they tried to bend the rules as best as they could. And the poor auditor who was totally under their thumb gave in."

US should provide definitive date for the use of IFRS

Will the US eventually convert to IFRS?

"The US Securities and Exchange Commission has committed itself to decide on US adoption of IFRSs during 2011, and I'm pretty confident that they will come on board. If they do, there will be a move by lots of the multinationals to go to IFRS as soon as possible. The real problem that is holding them back is that they haven't got a definitive date when the use of IFRS will be allowed in the US. The last thing they want to do is take a chance and then have to change all their systems back again. So, when they choose to switch to IFRSs, as I expect they will, a definite date needs to be agreed. Once the date is set, you will start finding major companies in the US using IFRS."

Implementation of IFRS means education in professional judgment

What changes will result from the implementation of IFRS in the US?

“When IFRS is allowed in the US, the US accounting profession will need to look at how to teach principle-based standards. And unless you get the American Institute of Certified Public Accountants (AICPA) churning out lots of guidance—which they say they don’t want to do—the accounting professionals are going to have to use their professional judgment.

“Now one of the big issues is what the former chairman of the FASB, Bob Herz, said: ‘We are going to have to educate the American accounting profession. This isn’t the way they have been taught.’ They were taught the rules at the university. So we are right back to the educational implications of this.”

Banks should not blame financial accounting but retain more reserves

Some of our other interviewees said that mark-to-market valuation maybe was not the cause of the recent financial crisis, but certainly exacerbated it. What do you think?

“Pretty much all of the post-crisis research has concluded that mark-to-market accounting did not play a meaningful role in the crisis, however we have worked with the FASB to provide additional guidance in how to apply mark-to-market accounting when the markets dry up. We’ve also simplified the financial instruments accounting standards, and as a result, it’s mainly anything held for trading, as well as exotic financial instruments that are subject to mark-to-market accounting—anything else would be measured at amortised cost.

“The real cause of the crisis was that during the good times, the banks paid out all their profits in three ways: either in dividends, buy backs, or compensation. They did not hold back enough in capital reserves, which is what you would have expected. They gave it all away. Banks’ capital was far too low for the lending they did—they made little effort to increase it in the good times. So, when the losses hit, they had no spare capital. What happened then, as you would have expected, was they had to sell assets to keep up their Basel ratios, and they sold into a falling market, which of course made it worse. And then they blamed fair value accounting. The accounting didn’t cause the losses, it simply described them.”

Use of expected loss model should increase accounting prudence

Should we use more conservative accounting again, restoring the prudence principle in its former glory?

“One of the problems that certainly came out of the financial crisis was the way the accounting recognized loan losses. While both IFRSs and US GAAP have broadly similar provisioning rules, US companies generally recognized the losses earlier.

The G-20, the Financial Stability Board, the Basel Committee on Banking supervision, and others have asked that we have a look at this, and as a result, we have recently announced joint proposals with the FASB to move to what is known as an expected loss model for loan loss provisioning.

Under an expected loss approach, when a bank issues loans in its portfolio, they are charging, let's say, 9% because they expect to get only 7% back. This is because they know some of those loans will go bad, but they don't know which ones they will be. The existing 'incurred loss' model requires the bank initially to book the entire 9% interest even though they know from experience that this figure is unrealistic. Under an expected loss approach, the accounting reflects the economics. You would not be able to book the full 9% in the first and the second year. You've got to put 9% in with a provision of 2% and build up the reserve earlier, but in a transparent way that is trued-up throughout the life of the loan. I hope we can stop provisioning so late because even now some of the losses haven't been recognized properly."

Narrative reporting useful to explain the implications of the raw numbers

How would you like to see business reporting evolve over the next 5 to 10 years?

"Accounting doesn't do things too well sometimes and that is why the narrative statement is going to be so important in addition to the raw facts. The notes to the financial accounts describe what has happened. They say, 'We got from here to there.' They don't say what the implications could be. That is why we need narrative reporting in which the board of a company is going to have to say: 'Let me tell you about these raw facts. The company looks like it has some problems, but this is how it will get out of them.' So my view is that financial accounting should show things in the raw, warts and all, and narrative reporting should say: 'Now, let me explain this to you.'

"Accounting doesn't do things too well sometimes and that is why the narrative statement is going to be so important in addition to the raw facts."

"As far as the UK pension funds, for example, were concerned, when companies started showing big deficits, the way they tackled it in their narrative report was to say, 'We have a deficit of 50 million. We expect the assets to rise at 4% per annum. We are going to inject an extra 9 million a year over the next few years. We expect to have cleared this deficit by 2013. Assuming profits stay at current levels, the negative effect would only be 1.2%.' End of story. What they are really saying is, 'This is how we are going to solve the problem.' And actually, that is what the analysts want to hear.

"So, I see narrative reporting becoming more and more important. And, frankly, the accounts could almost be an appendix to that, 'This is our financial position, now let me tell you about it!' And getting people to do that properly, without just boilerplate, will be tough. It is going to be one of the big challenges for the accounting profession.

"If we are going to emphasize the narrative report, then the auditors have to get on board. And how are they going to audit that? The world does not want the external auditor to be too guarded. Of course the auditor has to say, 'I cannot substantiate X and Y,' if that is the case, but investors would like to know from an auditor whether or not something is a reasonable comment to make. You will get lots of resistance. They are not going to want to do it, but the rest of the world will be supportive."

Unless we address litigation, management commentary is not going to make a lot of sense

Do you have any practical recommendations on how to avoid boilerplate in narrative reporting?

“A great concern is the question of litigation and the resulting need for safe harbors. Unless we can somehow protect the honest executive who makes his statement in good faith (which the auditors think is in good faith too) from legal action for misleading investors when what was predicted doesn’t come quite true, I think we are going to have a problem. So these directors are going to be very guarded and their lawyers will go all over it and their management commentary is not going to make a lot of sense. So I do think we need some protection for them, unless it is a willfully negligent statement.

“And the same concern also applies to the auditor. It is difficult for the external auditor to assert whether this narrative is consistent with the financial accounts. It would be quite nice, however, if we could think about ways in which the auditor could say, ‘This seems fair,’ as opposed to, ‘This seems not inconsistent,’ as we do it at the moment. And on that point, I think the present audit report needs addressing. It is just an excuse for why am I not guilty. In that respect, it was lovely to read the old audit report. It was only about three lines long, and when it was six lines, you knew it was qualified!”

After global convergence, simplification should be the next objective

How would you like to see financial accounting standard setting evolve over the next 5 to 10 years?

“My final point that I would like to make is that financial accounting isn’t rocket science, and we have had a tendency in the past to do things that are terribly complicated and that don’t need to be. The whole idea for the future is to make this as simple as possible. And some people will say, ‘He has had years to do this, what hasn’t he done it?’ It isn’t as easy as that, because we have had different objectives. Our job in the first few years was to patch up the standards in time for the first wave of jurisdictions to use the standards, then to improve them jointly with the FASB and to bring about their convergence. The objective for our successors’ Board will be to reduce the complexity—something that we will start but won’t be able to finish—and to remove the things of which investors think: ‘Why do we do it that way?’

“We should just make sure that people do understand it and that is why we have to get rid of very complicated standards like the deferred tax standard and the share-based payment standard. Before anyone gets too excited, we do need to measure these things, we just don’t need to do it in such a complicated way.”

Key recommendations from David Tweedie

1. To simplify financial reporting for (retail) investors, the accountancy profession should better define its terminology for non-accountants and reduce disclosure requirements to the bare essentials.
2. Mechanisms that allow companies to spread the effects of certain events, such as pension deficits, over longer periods should be removed from the financial reporting standards, because they mask the true financial position of a company.
3. Directors and auditors should take responsibility for financial reporting, using their professional judgment in applying principle-based standards, and acting upon the substance of a transaction.
4. Auditors should settle any interpretation questions with their clients using their professional judgment instead of asking the standard setters for additional rules, exceptions, and guidance to validate their assertion. Implementation of a principle-based standard, such as IFRS, means development of and education in professional judgment.
5. Investors should feel confident that the directors are in control. Companies, therefore, need non-executive directors who stand up against unacceptable accounting. The way companies appoint their non-executive directors is critical in this respect.
6. The US should set a definite effective date for the transition to IFRS, if it decides to allow the use of IFRS for US-based companies, so those companies can start preparing.
7. Banks should not blame financial accounting for their losses but should retain more reserves.
8. Management commentary should properly explain, without boilerplate, the implications of the raw numbers as described in the financial accounts, but unless we address litigation, management commentary is not going to make a lot of sense.
9. After global convergence, simplification of the financial reporting standards should be the next objective.

We welcome your feedback on these recommendations. To provide us with your feedback, please complete this brief survey.