

EFAA President, 4 Rue Jacques de Lalaingstraat, 1040 Brussels

European Commission

FAO Mr. Olivier Guersent

DG-FISMA

Financial Services Policy and International Affairs

1049 Brussels

Belgium

Bodo Richardt

President

4 Rue Jacques de Lalaingstraat

B-1040 Brussels

T +32 2 736 88 86

bodo.richardt@efaa.com

Brussels, 16 May 2017

Dear Mr. Guersent,

EC Public Consultation on the Operations of the European Supervisory Authorities

The European Federation of Accountants and Auditors for SMEs (“EFAA”) represents accountants and auditors providing professional services primarily to small and medium-sized entities (“SMEs”) both within the European Union and Europe as a whole. Constituents are mainly small practitioners (“SMPs”), including a significant number of sole practitioners. EFAA’s members, therefore, are SMEs themselves, and provide a range of professional services (e.g. audit, accounting, bookkeeping, tax and business advice) to SMEs. EFAA represents 17 national accounting, auditing and tax advisor organisations with more than 370,000 individual members.

EFAA would like to comment on Section 8 (financial reporting) of the consultation and specifically on questions 14 and 15. While we agree with the underlying motivation for the proposals – facilitating the closer integration of the financial markets in the EU through common rules and supervisory coordination - we do have some significant comments and concerns. Below you will find some general observations, including insights from some recent research we have conducted, and responses to the questions.

General Observations

ESMA’s Role in the Endorsement Process

We note that the consultation proposes to strengthen ESMA’s role in the endorsement process for International Financial Reporting Standards in Europe. We support the long-term objective of integrating financial markets in the EU because this brings significant benefits to the European economy. Integration requires common rules and supervisory coordination as the introduction to the consultation suggests. One

of the cornerstones of these common rules is a set of high quality financial reporting standards for Europe. In the current endorsement process EFRAG provides the European Commission with technical expertise and advice on accounting matters, including endorsement advice, successfully and in close and constructive co-operation with national standard setters (NSS). Furthermore, the ESA's are actively involved in the EFRAG processes where they provide valuable input that is duly taken into consideration. We see little if any reason to change this set-up as we explain below in our response to question 15. We are also somewhat surprised and disappointed to find that EFRAG and the existing endorsement process fail to be mentioned in the consultation. Furthermore, the consultation is absent a clear rationale, and supporting evidence, for the need to strengthen the role of ESMA in the endorsement process.

EFAA Research

EFAA published its report "[The Trickle Down Effect – IFRS and accounting by SMEs](#)" on 23 March 2017, presenting evidence for a process by which IFRS for listed companies are gradually introduced for smaller businesses through national GAAP. The corresponding [roundtable event](#) on 28 March 2017 attracted attention from international standard setters, the European Commission, Parliament, EFRAG and other key stakeholders. The research findings may, as explained below in the response to question 15, have implications for the endorsement process for accounting standards.

Specific Questions

14. What improvements to the current organisation and operation of the various bodies do you see would contribute to enhance enforcement and supervisory convergence in the financial reporting area? How can synergies between the enforcement of accounting and audit standards be strengthened? Please elaborate.

The former question seems to presume that improvements to the existing arrangements are necessary. We are not convinced that this is the case. Given the absence of evidence and explanations as to deficiencies of the current arrangements it is inappropriate and impractical to provide specific suggestions for improvement. In the first instance, we encourage DG-FISMA to define the set of objectives against which the actual outcomes are assessed. This might entail establishing some key performance indicators and corresponding targets. Only with such a gap analysis could one be in able to evaluate the existence and size of any gaps and discuss measures how to close them. Whilst one of these measures may indeed be a strengthening of convergence activities, it is by no means the only solution. The mere fact that convergence of the enforcement of accounting standards is limited does not of itself mean that the current system of

national competent authorities (NCAs) carrying out enforcement activities is not working. Moreover, even if there was evidence that it does not work in some jurisdictions, this is not a reason for automatically withdrawing enforcement and supervisory powers from all NCAs. Furthermore, the fact that ESMA cannot launch a breach of EU law case does not answer the question whether any such launch would have been deemed necessary but had been prevented. Again, the consultation paper is silent on whether such a case exists. Hence, we are not convinced that strengthening enforcement powers is warranted without having seen evidence that there are deficiencies or weaknesses that need to be addressed.

The latter question fails to specify what synergies the Commission has in mind. As far as we can tell, the enforcement of accounting standards in at least some Member States in which EFAA has members appear to work effectively. In respect to audit standards we note that a long debate about the appropriate setup of audit supervision in Europe has recently ended and concluded that no pan-European agency was necessary in the field of audit regulation and supervision. Hence It is premature to re-open the debate especially in the form of a regular consultation on the operations of the ESAs. We believe that the agreed-upon structures need to be given time to see whether they are working as expected or whether changes are warranted. During this time, we encourage those responsible for the enforcement of accounting and audit standards to share experiences and lessons so that they might learn from each other and investigate the merits of collaboration.

15. How can the current endorsement process be made more effective and efficient? To what extent should ESMA's role be strengthened?

This question, like question 14, appears to presume that the current endorsement process needs to be made more effective and efficient. We are not convinced that this is the case. Given the absence of evidence and explanations as to deficiencies in the current endorsement process it is inappropriate and impractical to provide specific suggestions for improvement. We note that the European Commission has recently conducted a comprehensive review of the functioning of the IAS Regulation and that this review did not reveal the need for change. To the contrary, the conclusions were positive and the vital and valuable role of EFRAG was confirmed. Furthermore, the majority of the recommendations of Philippe Maystadt, Special Advisor to the European Commission, for enhancing EFRAG's set-up and processes have been fully implemented and are working well. While Maystadt did express a personal preference for the integration of the endorsement and enforcement process under ESMA he declined to recommend such an integration in the face of overwhelming opposition from stakeholders. These stakeholders preferred that EFRAG reform its endorsement procedures rather than surrender its endorsement role. This opposition was justified at the

time and remains valid for the following considerations:

- *Accounting standard setting (including the endorsement of standards) is a legislative process in the context of the IAS Regulation. Such a legislative function is best kept separate from the enforcement role of ESMA that addresses proper application of the accounting standards.*
- *Accounting standards should be developed bearing in mind the interests of all stakeholders (including employees, suppliers, management and government) and not only those of capital market participants. EFRAG's current public-private sector model ensures that all stakeholders with an interest in financial reporting are involved in the process and that EFRAG works in the public interest. This is reinforced by EFRAG's due process which collates input from all stakeholders. EFRAG provides an important platform to all NSS through its Consultative Forum of Standard Setters and ensures that the views of smaller NSS are considered during the formulation of European positions.*
- *Non-endorsement of standards is not the desirable outcome of the endorsement process. To allow the International Accounting Standards Board to develop high quality financial reporting standards that meet European needs and that are fit for endorsement requires early involvement in the standard setting process and pro-active research work to ensure that the needs and interests of Europe are understood in the international financial reporting debate. This work is being carried out successfully by EFRAG and for it to be credible and influential should not be disconnected from the ultimate endorsement advice. The endorsement advice function enhances EFRAG's ability to influence and ensure that European views are fully considered in the IASB's standard setting process.*

EFAA believes the current endorsement process satisfies these considerations and is generally working well. Our only suggestion is that the endorsement process be refined to enhance efficiency. Presently it sometimes takes considerable time to consider in depth amendments that are largely uncontroversial in terms of the endorsement criteria. Such matters, perhaps determined using some simple criteria, deserve to be expedited. There is no reason nor evidence to suggest that there is a need to strengthen the role of ESMA. Therefore, we feel that more time is needed to accumulate evidence before one can fully evaluate the effectiveness of changes prompted by the Maystadt reform.

As mentioned under 'General Observations' above EFAA has recently published research relevant to this consultation. Accounting rules for SMEs in Europe are set by the requirements of the European Accounting Directive, supplemented by national Generally Accepted Accounting Principles (GAAP). However, the directive is silent on how to account for certain matters, such as the definitions of assets and liabilities,

accounting for leases and accounting for pension obligations. In such instances, national GAAP will often be developed – and this may potentially follow IFRS. EFAA wanted to see the extent to which this has been happening: if IFRS treatments do ‘trickle down’ to the level of SME accounting. The paper reveals strong evidence of a trickle-down effect. This begs the question whether, and if so how, might the existence of the trickle-down effect warrants consideration as standards for listed companies are developed and endorsed.

I trust that the above is comprehensive but should you have any questions, please contact me any time.

Yours faithfully,



Bodo Richardt

President