Remarks by Leslie F. Seidman
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Introduction

Good morning.

It's a pleasure to be back in Washington as part of this outstanding conference. When I flipped back the pages of my calendar for the last 12 months, I was struck by the number of significant issues we have all dealt with and how much we have accomplished. I appreciate that the people in this room played an active role in making that happen. I explained to Hans, that the people who come to this conference are accountants, auditors and other professionals in our field who are deeply engaged in the process, are who truly care about financial reporting. This morning, I'd like to discuss some of the important developments of the past year, and also raise some issues for us to consider over the next year. I'll speak for about 25 minutes, then Hans will speak, and then we will be happy to answer your questions.

Before I go further, let me remind you that the remarks I make today reflect my own personal views, rather than official positions of the FASB.

I think there are two elephants in the room with us today (and I don't mean anything partisan by that): One is international accounting standards, and the other is private company reporting. Fortunately, this is a very, very large auditorium, so I think there is room for all of us. These are two of the most important issues facing our profession, our capital markets, and our companies, so I think it's important for us to have a frank, constructive discussion of them.

Let me set the stage for the discussion. The reason we have accounting standards is to provide information that is useful to existing and potential investors and other users of financial reports in making decisions about whether to provide resources to the company or nonprofit organization. That's straight out of our new, converged concept statement on the objectives of financial reporting.[1] Large, global investors and smaller domestic lenders want to be able to pick up a financial report and have some degree of assurance that the same transaction will be accounted for consistently from company to company. So the goal of accounting standard setting is customer driven, or, put another way, user focused.

Companies play an important role, because they are generating the transactions, and have to implement the standards. Likewise, auditors have to express an opinion about the company's application of the standards, so their views must be considered as well. The entire process involves balancing the benefits to the resource providers with the costs of providing – or *not* providing – the information. But make no mistake: the primary goal of financial reporting is to assist the people trying to make decisions about whether and how to invest their money.

While it might seem obvious, I'm afraid this goal gets lost in the debate on both of these subjects at times. Yet, it lies at the core of how we at the FASB think about both the international accounting and private company issues.

International Accounting Standards

Let's talk first about international accounting standards.

The FASB has long supported the goal of developing high-quality, comparable, global accounting standards. Let me quote from our 1999 Vision Statement on International Accounting Standard Setting[2]:

"…the FASB's objective for participating in the international accounting standard-setting process is to increase the international comparability while maintaining high-quality accounting standards in the United States."

I'll call this the dual objective.

[1] FASB Concept Statement No. 8, *Conceptual Framework for Financial Reporting*, September 2010.
[2] *International Accounting Standard Setting: A Vision for the Future*, FASB 1999.

The Vision Statement also describes the attributes of a high-quality standard:

1. It is consistent with an underlying conceptual framework
2. It avoids or minimizes alternative accounting treatments, because comparability enhances the usefulness of information
3. It is unambiguous and comprehensible, for those who must apply the standard, enforce it, and use the resulting information
4. It is capable of rigorous interpretation and application so that similar events and transactions are accounted for similarly across time periods and among companies.

Each of these attributes promotes the relevance and comparability of financial information.

The FASB's dual objective of converging and improving financial reporting in the U.S. guided the selection of the topics for the original memorandum of understanding (MOU) between the FASB and IASB. In other words, those standards were not just different, but they were viewed by both boards as needing improvement as well.

Clearly, we have made significant progress together in narrowing the differences between U.S. GAAP and IFRS – and we have improved the standards at the same time. For example, we have substantially converged our standards on business combinations, noncontrolling interests, fair value measurements, borrowing costs, segment reporting, and many others. Let me take this opportunity to thank Sir David Tweedie and Bob Herz, who were at the helm when the vast majority of this work was completed, as well as our terrific staffs.

We still are working hard to address other very important projects, including revenue recognition, leasing, financial instruments, and insurance contracts. As you may know, we just issued a second exposure draft on revenue recognition, which proposes a new, converged standard. Despite the challenging nature of these topics, and the various views held around the world, I am optimistic that ultimately, we will be able to resolve our differences on all of these topics and establish improved, converged standards in these key areas. Our Technical

Directors, Sue Cosper and Alan Teixeira, will talk about these topics in more detail, later today.

But where do we go from there?

In thinking about convergence, you might relate to the words of the American poet, Ogden Nash, who said, "Progress might have been alright once, but it has gone on too long."

Despite its challenges and, in retrospect, its overly ambitious scope, I think the convergence process has advanced global financial reporting in several key areas. However, I believe that the side-by-side convergence model is not the optimal model in the long run.

At this conference last year, Paul Beswick of the SEC staff introduced the "condorsement approach," which was later issued in more detail as an SEC staff paper[3]. The paper explored a very different approach to convergence and incorporation of IFRS, and a new role for the FASB. So naturally, the FASB and the FAF Board of Trustees, FASB's oversight organization, were very interested in the constructive responses sent to the SEC staff on this potential approach.

Last month, the Chairman of the FAF, on behalf of the Board of Trustees, and in consultation with the FASB, submitted a letter to the SEC supporting a condorsement approach with some recommended modifications and clarifications intended to address the concerns that were raised by many who offered comments to the SEC staff.[4]

Our letter expresses strong support for IFRS becoming the foundation for future accounting standards, but also offers constructive suggestions to mitigate the transition risks that have been identified. In other words, we suggested a modified incorporation approach that could potentially gain broad support in the U.S.

[3] SEC Staff Paper, *Exploring a Possible Method of Incorporation,* May 26, 2011.

[4] Brennan, John J., Letter to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, November 15, 2011

The path recommended by the Trustees would incorporate IFRS into U.S. GAAP over time. The key elements of the approach recommended by our Trustees, and strongly supported by the members of the FASB, are:

1. The FASB and IASB would complete the priority convergence projects with the IASB.
2. The U.S. would look to the IASB to set new accounting standards, and we (collectively) would participate actively in that process, in order to be in a position to endorse the final standards for incorporation into U.S. GAAP. The key elements of the process include investor primacy, independent standard setting, robust due process, a considered cost-benefit analysis, and clear and adequate guidance.
3. We would keep the label "U.S. GAAP" to avoid several practical problems, such as the need to change debt covenants, which often refer to U.S. GAAP as a benchmark.
4. The FASB would evaluate the remaining differences between U.S. GAAP and IFRS, and develop a plan to address them. This is a transition matter, but obviously, a very important element of the overall plan.
5. The FASB would retain the ability to set standards for the U.S., if there are topics of considerable importance that are not on the IASB's active agenda or if the IASB doesn't provide timely or adequate implementation guidance.

Let me elaborate on the rationale behind each of these elements.

First, the convergence phase. We would very much like to work together with the IASB to complete the priority projects on revenue recognition, leasing, financial instruments and insurance. However, we do not believe indefinite convergence is a viable option, politically or practically. As any observer can see, this process is challenging technically and administratively. Plus, we appreciate that the IASB, as an international body, must be responsive to the priorities of other countries that have already adopted IFRS.

Second, we would look to the IASB to set new accounting standards for the U.S. This would put the U.S. on record as accepting IFRS as the basis for its accounting standards, moving forward. The FASB would refrain from setting standards that are on the IASB's active agenda, and would not be at the table debating new issues jointly. The FASB would, however, play a key role in gathering input, conducting research, coordinating field work, assessing the need for implementation guidance, and managing post-implementation reviews with U.S. stakeholders. The idea is that the IASB would participate in these activities, but FASB would be the focal point for coordination in the U.S.

This type of role is supported by other national standard setters, because in order to ultimately endorse a standard for your country or region, you have to have been an active participant in these processes yourself.

The benefit of a strong role for the FASB and other U.S. stakeholders is that, as active participants, we are more likely to be satisfied with the process, so that in the end, we would be much more likely to endorse the standard. Having said that, we envision that we would only endorse a change in a major standard that represented an improvement in reporting for our investing public and that could be implemented by our companies and audited by our auditors at a reasonable cost. As I said at the beginning, this has always been our dual objective. In this context, we are simply acknowledging that we have extensive experience in our marketplace, and we are best positioned to understand or translate the perspectives of U.S. stakeholders.

I would also observe that the IASB can continue to leverage the talent and resources of strong national or regional standard setters to advance the development of standards. For example, the IASB has agreed to consider the disclosure framework that we are developing in cooperation with European Financial Reporting Advisory Group as the basis for a future concept statement or standard about disclosure.

Regarding the evaluation of the remaining differences, the U.S. is in a different starting point than other countries. Let's face it—we have a lot of GAAP, whether you like it or not, and whether all of it applies to you or not. I believe it is *not* in the best interest of our investors to withdraw GAAP in areas where there is no clear accounting standard under IFRS, such as in the case of rate regulation. That means we would be following U.S. GAAP in some areas until the IASB takes on a project and sets a new standard for the world.

I have heard some say that as long as our standard doesn't conflict with IFRS, we could still say we are following IFRS. Frankly, I don't understand how that is transparent to global investors, when others around the world would *not* be following our U.S. GAAP standard. I would rather be forthright, identify the standards we are keeping as a matter of transition, and whittle down the list as the IASB addresses those issues. I think it is a disservice to investors to *say* we have a single global set of accounting standards when significant differences remain below the surface.

Regarding the cases where we both have standards, but they are different, I would look at the remaining differences and ask: are these differences important?

- Clearly, some of them are. For example, the difference between U.S. GAAP and IFRS on research and development is a core issue for some companies and their investors.
- Likewise on recycling amounts out of other comprehensive income (OCI) to net income. We Americans recycle those amounts; under IFRS, most items of OCI are not recycled.

I would envision that when we think the IFRS standard is of the same quality as U.S. GAAP, we would propose adopting the IFRS standard. In those cases, the improvement comes from having global comparability, as opposed to the standard itself. Where we have concerns about the quality or operationality of an IFRS standard, we might ask the IASB to take on an issue before we incorporate it. Ideally, there would be a match between our requests, and those of other countries. For example, we understand that other countries also would want to revisit recycling and the accounting for loss contingencies.

I think we also have to consider the differences in our XBRL taxonomies. Our U.S. GAAP Taxonomy is significantly larger than the IFRS taxonomy in part, because we have more expansive GAAP requirements, but also, because we have incorporated the elements commonly used in practice. Our outreach to data aggregators and analysts indicates that they find these common elements extremely helpful, as opposed to having to deal with large volumes of customized tags, or worse, the normalization that can occur when companies decide that an existing tag is “close enough.” Obviously, the most effective way to approach this depends on the path taken relating to incorporating the related standards.

We also have learned that there are differences in the way the international standards are applied, and it is important to understand why--

- The standard could permit alternatives, or be too general in nature.
- The companies might not apply the standard as it was intended.

The recent SEC staff analysis of IFRS in practice[5] discusses these issues in more detail. But regardless of the reason, we would seriously question the cost-benefit of switching our country to a standard that we know is not applied consistently around the world. I have heard people say: “There will always be differences in the way companies apply a standard, even if it is U.S. GAAP.” True enough, but we are talking about a significant cost to make the change; it seems to me that the benefit of global comparability should be real in order for us to conclude that it is worth the cost of making the switch.

If the SEC were to decide to move forward with an approach like the one outlined by the FAF Trustees, the FASB would establish a framework to identify these various types of differences, and then develop a plan for the best way to resolve them. Clearly, we would seek broad input on that analysis. And let me assure you, we would be looking for ways to make the process as efficient as possible.

And last but not least, the Trustees are recommending that the FASB would retain the ability to set its own agenda of technical matters that are not on the IASB’s active agenda. This is perhaps the most controversial point internationally, because it is sometimes understood to undermine the goal of a single set of

[5] SEC Staff Paper, *An Analysis of IFRS in Practice*, November 16, 2011.

standards. As one European accountant expressed it to me, we seem to be saying, “Yes….but no.” Here’s the way I think about it.

We always are going to need a nimble, responsive body to address important matters in the U.S. In cases where other countries share the issue, we would hope to convince the IASB or IFRIC to take up the issue and then participate in the process. But, if they don’t, we would address the issue for the U.S., and then the IASB could later consider the standard for broader use.

There are a couple of things to think about here. The IASB is in the process of a global agenda consultation, which has been long awaited by many parts of the world. We would expect the IASB to add projects to address those regional concerns. Second, many parties are calling for a period of calm to allow them to transition to the new standards, and for the IASB to focus on the Conceptual Framework for the next few years. But I have yet to experience a period of calm as an accountant in the U.S., and I expect pressing matters to continue to emerge that require our prompt attention. So you can think of this as a safety net if you like, but something that is very important in our culture.

In my view, this approach would show strong support for the IASB regarding the establishment of new global standards that the U.S. would follow, and would employ a rational transition process for continuing alignment of our legacy standards.

I have great respect for the SEC commissioners, the SEC staff and the process they have followed to date to address this important issue. I hope they view our comments as constructive and helpful as they move forward in their evaluation of the best approach for our country.

Private Company Accounting

Now let me turn to the other elephant in the room, private company accounting. Given the fact that this is an SEC conference, I am assuming that many of you work for or audit public companies. You may think the private company issue doesn't affect you. Yet, I would imagine that some of you are users or auditors of the financial statements of private companies, when your company or client is a lender, a vendor, a supplier, or an equity method investor. I would like to share my perspectives about why I think it is an important issue for all accountants and investors, whether you are currently working with public companies or private companies.

It goes back to the point I made at the beginning about the purpose of accounting standards. Accounting standards are meant to provide useful, comparable information to potential and existing investors, lenders, and other users of financial statements to help them make an informed decision about whether to provide resources to the reporting entity. That should always be our guiding principle, but we should also take care to make sure that the standards are understandable, and able to be applied consistently and at a reasonable cost.

We have heard significant concerns expressed by private companies in recent years that some standards are not providing relevant information, and that some standards are too complex and costly to apply. Clearly, we have heard similar concerns from public companies, and of course, the SEC's Committee on Improvements to Financial Reporting from a few years ago recommended reducing unnecessary complexity in standards.

So is there a unique issue here for private companies? We have been working very hard to figure that out. We are conducting a significant amount of outreach, in the form of meetings and roundtables to understand the distinguishing factors for private companies and how they might influence the standard setting process.

We learned that there are six factors that private companies seem to agree distinguish them from public companies.[6] The two I'll highlight are:

- The primary users of private company reports are lenders, not external equity investors
- Management can provide any information it wishes to a current or potential lender or investor (that is, they are not subject to Reg FD[7]).

[6] FASB in Focus, *Private Companies: The Path to a Differential Standard Setting Framework,* July 11, 2011.

Our staff is taking all of the feedback we have heard, and developing modules that explore how the distinguishing factors should affect the key types of accounting issues that we deal with, including recognition, measurement, disclosure, transition, and even effective date.

For example, does the ability of management to freely provide additional information mean that mandatory disclosures should be reduced for private companies? We will develop these guidelines with the advice of a resource group and our advisory councils and then expose them for public comment. (By the way, we would not plan to finalize them without the buy-in of any new group set up to focus on private company issues.)

In my view, this analysis is essential to make informed, consistent decisions about when differences should be made for private companies. I think it is crucial to sort out the issues that relate to what information is relevant from the issues that relate to complexity or excessive cost. Relevance is the number one qualitative characteristic of financial reporting. Therefore, if we identify differences in what is relevant to users of private company financial statements, I think a difference in accounting is justified. But if the issue primarily relates to complexity or cost, it is not obvious to me that the solution is an exception for private companies. My hunch is that everyone could benefit from simplification. For example, the concerns we heard about the complexity of the first exposure draft on revenue recognition were shared by public and private companies. The revised ED hopefully reduces complexity for everyone.

We also have made numerous changes to improve our ability to understand the private company perspective, including staffing changes, as well as more regular outreach to private companies through roundtables, participation in conferences, electronic feedback forms for our proposals, educational webcasts and other means. We have been demonstrating on a daily basis that we want to do the best possible job for our private company stakeholders.

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[7] Fair Disclosure, SEC Regulation FD, August 15, 2000.

Nonetheless, many are still concerned that these improvements are well intentioned, but possibly fleeting as the current board and staff members turn over. So, as you are no doubt aware, the Blue Ribbon Panel[8] recommended to our Trustees, among other things, that a new, separate board be established to set GAAP for private companies. After significant consultation with a wide variety of private company stakeholders, our Trustees acknowledged that there was a need for sustained, increased focus on the private company perspective, but decided to propose a different structural change. They are proposing a Private Company Standards Improvement Council that would be chaired by a FASB member, and the Council would report to the FAF Board of Trustees. Using an agreed-upon framework, the PCSIC would evaluate existing standards and future standards, and identify cases where some or all of a standard should be different for private companies. All FASB members would attend the meetings, and listen to the discussion first hand. The PCSIC would vote, and then their decisions would be ratified by the FASB, similar to the current situation with the EITF.

Underlying this recommendation is the FAF's belief that over time, the standards of two entirely separate boards will inevitably diverge, despite their best intentions. Hans and I lead two boards with a serious desire to reach the same conclusions, and yet we do not always agree. This does not mean that the FAF thinks there should never be differences. Rather, by integrating the activities of the PCSIC and FASB, any changes that aim to reduce complexity can be considered for all entities, and the differences can be limited to those distinct private company characteristics.

I would encourage all of you to share your views with the FAF on this important issue, by January 14. I would ask you to focus on the needs of the users of financial statements, as well as the FASB's willingness to tackle the complexity issue for all stakeholders.

In closing, let me repeat that our mission, at its most basic level, is to develop accounting standards that empower investors and other users of financial

[8] Blue Ribbon Panel on Standard Setting for Private Companies Report to the Trustees of the Financial Accounting Foundation, January 2011.

statements by promoting neutral, understandable, and comparable financial reporting.

The approaches I've outlined today toward incorporating IFRS into U.S. GAAP and focusing more attention on private company reporting issues both are intended to promote greater comparability while maintaining high-quality accounting standards. But they also are intended to ensure that issues specific to individual constituencies are recognized and dealt with in a way that does not unnecessarily increase cost or add complexity. I know that there are differing views on how we should best pursue these objectives, both on the international front and for private company constituents. The beauty of our process is that all of those views will be carefully considered.

However, my goal today was to explain why the FAF and the FASB believe that the path to international accounting standards – and to addressing the needs of private company stakeholders – that I have outlined today would best enable us to fulfill our mission in the current environment.

Thank you for your attention. Now, I'd like to welcome Hans Hoogervorst to the podium.