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Dear Ms Kerr

LOUDER THAN WORDS: PRINCIPLES AND ACTIONS FOR MAKING CORPORATE REPORTS LESS COMPLEX AND MORE RELEVANT

The Global Accounting Alliance (GAA) is pleased to respond to your request for comments on the discussion paper, *Louder than Words: Principles and Actions for Making Corporate Reports Less Complex and More Relevant*.

The Global Accounting Alliance

The Global Accounting Alliance (GAA) was formed in November 2005 as a grouping of leading professional accountancy bodies in significant capital markets. It was created to promote quality services, share information and collaborate on important international issues, whilst operating in the interest of a quality accounting profession and the public interest. The Alliance works with national regulators, governments and stakeholders, through member-body collaboration, articulation of consensus views, and working in collaboration, where possible with other international bodies, especially IFAC. The GAA member organisations represent around 775,000 professional accountants in over 165 countries around the globe.

Further details are provided in the Appendix to this letter.

General Points

Introduction
The GAA welcomes this initiative from the FRC and is in general supportive of the discussion paper ("DP"). In particular, we welcome the view taken which emphasises a principles based approach and aims to support businesses by enabling them to present their financial statements in a clear, uncomplicated and effective manner and one which portrays a transparent and unambiguous view of their performance.

It is important that, as far as possible, the complexity of corporate reporting should be reduced and its relevance increased. Complexity in reporting and regulation imposes costs on users of financial reports who have to invest considerable time in seeking to understand corporate reports and the rules which underpin them, and there is a risk that important messages will not be identified or understood. In our view, the discussion paper (DP) provides a useful analysis of the issues and some interesting ideas on how progress can be made.

Relevance
The DP's title indicates that it is intended to cover both relevance and complexity. However, the emphasis appears to be more on the latter. The inclusion of irrelevant information in reporting certainly exacerbates the problem of the volume of detail in financial statements and to that extent makes them more complex. It may therefore be appropriate for the FRC to consider the question of relevance further in a separate publication.

Follow-up
We note that the DP lacks a list of specific action points to be undertaken and we would draw your attention to the need for some firm proposals to arise from the outcome of the consultation process. Many of the potential actions would seem to lie in the hands of third parties, and it would be helpful to know what the FRC itself plans to do – by way of its own actions and by way of encouraging those third parties to take the necessary actions.

Users
We note that the users to whom the FRC spoke in preparing the DP 'do not consider [annual reports] too complex overall': on the evidence of the DP, concerns about complexity seem to lie much more with preparers. If the FRC's DP is correct, this suggests that the problem is different from that which had been assumed. This was mirrored in the GAA's research mentioned below but only to the extent that, whilst users considered the financial statements to be long and complex, there was an assumption that some of the complexity was inevitable and was therefore accepted.

Corporate reporting attempts to reach a number of users, and therefore, is not targeted at the needs of a single specific user. This leads to financial statements being more complex because of the need to cater for a wide variety of information needs, both in terms of depth of detail and breadth of information. Even the more sophisticated users of financial statements can be sub-categorised into distinct and important groups which may have very different needs. Not only are there different equity investors and their advisers – tracker and index funds, long-term value investors, day-traders/short-sellers and arbitrageurs, buy-side/sell-side analysts – but there are also important debt-related users, such as credit rating agencies and the like. The type, extent and complexity of information that these users want from the annual report may vary considerably, and yet all are purported to be served by general purpose financial statements under the IASB Framework. Therefore the discussion on page 10 on 'Remembering who the users are' may need to be more sophisticated in considering who the users are who have a legitimate interest in the annual report.

It also needs to be borne in mind that users' requirements for relevant information are met in a variety of ways, and not just from annual reports.

Can Financial Reporting be made Simpler and More Useful?

The GAA in its report *Getting to the Heart of the Issue: Can Financial Reporting be made Simpler and More Useful?* highlighted the results of its interview based research on the subjects of (i) principles vs. rules in financial reporting and (ii) complexity and detail in financial statements. In relation to the latter topic, some of the key messages emerging from the research were:

The problem

- Financial statements are generally regarded as long and complex;
- Users appear to find it difficult to identify the really important information or understand the "essence of the business" from the financial statements;

Reasons for complexity and detail

- The complexity of financial statements reflects businesses, transactions, and a business environment which have become more complex;
- Complex language is sometimes necessary to allow specialists to communicate in an effective manner;
- Accounting standards introduce complexity through convoluted accounting methods, such as in the areas of stock options, pensions and leases;
- Additional disclosures are required to compensate for accounting treatments which are complex and not transparent;
- Detailed disclosures often appear to be driven by the desire to limit the company's liability rather than adding greater clarity;
- Disclosures are often needed to explain the volatility inherent in the financial statements;

Users' needs

- Simpler, shorter financial statements are more likely to be read, but specific items of detailed information can often appear to be relevant, especially in retrospect;
- There are a number of different user groups whose needs can be very different and who rely on the financial statements to varying degrees;
- Sophisticated users often want more information, whilst individual investors find the financial statements too long and complex;
- Preparers can find it difficult to judge what is important to users;

Possible solutions

- New technologies such as XBRL could facilitate a layered reporting solution for different levels of investor, with a high level set of printed financial statements and additional information available on a drill-down basis on the company's website;
- Simpler, more straightforward language should be used, with less jargon and "coded language";
- Management commentary and non-financial information should assist in providing a good sense of the business and how it is performing: the style of Warren Buffett's letters to shareholders was commended by many.

These results certainly lend support to the publication of the FRC's discussion paper. As a result of the GAA research, three Roundtable discussions were subsequently held in London (March 2009), Beijing (April 2009) and New York (July 2009). These considered a number of suggestions arising from the project, including the following:

1. Should a single definitive set of general purpose financial statements be retained?
2. Should standard setters be encouraged to drop requirements considered redundant?
3. How can company boards be encouraged to provide better quality communication?
4. Should an international framework for high level summary financial statements be developed in order to provide information suitable for retail and less sophisticated investors?
5. Should general purpose financial statements be developed and published in XBRL format to allow users to drill down to whatever level of detail is required?
6. Should company communication be improved through the use of clearer language, less jargon and coded language, and a focus on clarity and transparency?

The GAA is due to issue a report within the next few months to communicate the major points and areas of consensus emerging from these events. We would be pleased to send a copy of this report to the FRC, and to other commentators on request.

Specific Questions:

Q1. Can the principles for less complex regulation we propose help reduce complexity? Are there other principles that should be considered?

In our view, the four principles proposed would help to reduce complexity - if they were able to be put into effect. Having regulation that is targeted; proportionate; co-ordinated and clear and which helps to produce financial statements that have the same characteristics can in our view only be a positive influence on financial reporting in general and should help reduce the complexity we have at present.

We suspect that most regulators and standard setters would in fact be happy to subscribe to the four principles and may indeed believe that they already comply with them. However, we question whether one set of principles will be sufficiently comprehensive for all of the respective regulators and users of financial statements, given the differing information needs.

In the longer term, we believe that the length (and therefore the perceived complexity) of the printed annual report could be reduced if some or all of the information currently included in it were made available only on the company website, which could be accessible for reference purposes. The printed report could therefore be significantly reduced, to focus on the higher level informational needs of the wide group of users and to allow the management to communicate that information which they see as key to an understanding of the performance of, and prospects for, the company. The existing full annual report could be made available electronically on the company's website, and this could in future be expanded and developed using technologies such as XBRL to facilitate better access to that information and possible drill down to obtain further detail for those who desire it.

Q2. Targeted: Is cash flow reporting in need of improvement? If so, what is the best means of achieving this improvement? Consider changes to IFRS, best practice guidance, publicity campaigns, other.

This is an important question, and we would support the FRC in its actions to launch a project to further investigate users' needs for cash flow and net debt reporting. The best way of making any changes would be through amendments to IFRS.

Q3. Proportionate: Should accounting standards and other regulations be based more on the information that management produces internally?

In principle, we believe that it is desirable that external reporting should be fairly well aligned to internal management information, to reflect the way in which the business is operated. However, it should be borne in mind that:

- information in businesses is produced for a variety of reasons and to varying degrees of detail, and much of it will not be suitable or relevant for the purpose of inclusion in the financial statements; and
- internal management information varies from company to company, whereas accounting standards are intended to reduce variation to provide a degree of comparability between companies for external users.

Q4. Proportionate: Would a project on disclosures help stem the constant growth of accounting disclosure requirements? Could it also identify the most important disclosures, with a view to giving them greater prominence?

We would agree that a thorough review on disclosures would be helpful, but any review must be mindful of the fundamental principle that different users of financial statements will have different views on what they would regard as the most important disclosures. A balance would have to be struck here that seeks to keep the financial statements at a readable, manageable size whilst at the same time not diluting the quality of the information they contain. This is an area where there is an onus on the companies themselves to be more proactive in distinguishing material from immaterial disclosures.

It will not be easy to stem the growth of accounting disclosure requirements, which is often in response to demands from various users. We note that the FRC's own list of opportunities for further action includes calls for additional disclosures on some matters. There could also be situations where certain investors may be unwilling to forfeit any information which they currently receive.

As noted in our response to question 1 above, in the longer term the length of the printed annual report could be reduced if information currently included in it were made available for reference purposes on the company website instead.

Q5. Targeted and proportionate: Who are the main users of wholly-owned subsidiary accounts? Should the subsidiaries be required to file audited accounts with full disclosures? Is a more simplified reporting regime appropriate?

Large groups can have hundreds of subsidiaries, for which financial reporting takes a great deal of group time and effort. The decision to create such complex structures is presumably driven by considerations such as tax and liability management, and it is not clear that financial reporting requirements should be simplified, potentially to the detriment of creditors, where the group has chosen to structure itself in this way. Other users of the accounts of wholly-owned subsidiary companies are likely to be lenders, customers, suppliers, employees and tax authorities, and it could be argued that these should not be disadvantaged by not having full accounts available.

As a global body, we observe that there are likely to be very different perspectives on this question in different countries around the world.

Q6. Targeted and proportionate: Would it be desirable to eliminate the UK requirement to prepare, have audited, and file wholly-owned subsidiary accounts in the case of a parent company guarantee?

We do not wish to comment on the specific circumstances of the UK, beyond those comments set out in response to question 5 above.

Q7. Coordinated: Would it increase or decrease complexity if national and international regulators worked together in a more joined-up way? Is there a risk that international regulators working together might result in imported complexity for some jurisdictions? How do we mitigate this risk?

As the question indicates, working together by international regulators may import higher levels of complexity for individual countries. However, we are fully supportive of moves towards a single global set of principles based financial reporting standards, and of national and international standard setters and regulators working together to achieve this common goal. We would support an increased focus for the IASB in seeking to reduce complexity even if different jurisdictions, which have very different approaches to financial reporting and different legal approaches, find that they need to impose some additional national requirements.

Q8. Clear: Would an emphasis on delivering regulations and accounting standards in a clear, understandable way reduce complexity? How can we move best towards clearer regulations and accounting standards?

There is a need here to stand back and gain an understanding of what the various users want out of a set of financial statements. It is only after this is clearly understood that regulators can set about delivering clearer regulations and accounting standards.

It is difficult to see how clearer drafting can be institutionalised. Poor or complex drafting is common in many areas of regulation and legislation, and the profession and business community needs to constantly monitor proposed standards and regulation and ensure that adequate and genuine consultation takes place.

Q9. Do you agree that the principles for effective communication can reduce complexity in corporate reporting?

We believe that applying the principles for effective communication should reduce the complexity in corporate reporting. However, this relies on companies genuinely embracing the principles and the spirit of those principles, in both good times and bad times. We note that increased openness and transparency will often add to the length of reports: but while length and complexity are different, we suspect that for many people increased length effectively means increased complexity.

Q10. What are the barriers to more effective communication? How might these barriers be overcome?

We believe that there are four main barriers to effective communication:

- lack of time – it takes more time to draft concise quality reports;
- lack of ability – drafting quality communications is a skill which many may not possess or wish to buy in;
- motivation – management can be influenced by the desire to present a positive view to shareholders and other users;
- legal liability – failing to meet all legal and regulatory requirements, or making statements which could be seen (in retrospect) to mislead, may damage a company's reputation and lead to financial penalties and/or legal action.

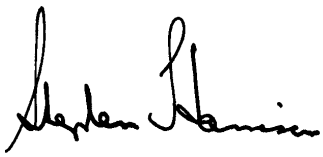
We are unable to suggest any single way of overcoming these barriers. However, over time, we would hope that the communication culture may improve, through regulators such as the FRC encouraging companies to adhere to these principles and supporting companies by regulating them in a proportionate and outcome oriented manner.

Q11. Which of the specific sources of complexity in corporate reports noted on pages 54 to 55 warrant further action? Which organisation(s) would be best placed to assist with the necessary action?

We have no comment to make on this section.

We hope that our comments are helpful to you in taking these important issues forward. Should you wish to discuss any of the above points further, please do not hesitate to contact me or David Wood at ICAS, project leader for the GAA report referred to above.

Yours sincerely



STEPHEN HARRISON AO FCA FAICD
Chief Executive Officer

APPENDIX

THE GLOBAL ACCOUNTING ALLIANCE

The Global Accounting Alliance (GAA) was formed in November 2005 and is an alliance of leading professional accountancy bodies in significant capital markets. It was created to promote quality services, share information and collaborate on important international issues. The Alliance works with national regulators, governments and stakeholders, through member-body collaboration, articulation of consensus views, and working in collaboration, where possible with other international bodies, especially IFAC.

The Alliance facilitates a co-operation between eleven of the world's leading professional accounting organisations:

- American Institute of Certified Public Accountants (AICPA)
- Chartered Accountants Ireland (CAI)
- Canadian Institute of Chartered Accountants (CICA)
- Hong Kong Institute of Certified Public Accountants (HKICPA)
- Institut der Wirtschaftsprüfer in Deutschland (IDW)
- Institute of Chartered Accountants in Australia (ICAA)
- Institute of Chartered Accountants in England and Wales (ICAEW)
- Institute of Chartered Accountants of Scotland (ICAS)
- Japanese Institute of Certified Public Accountants (JICPA)
- New Zealand Institute of Chartered Accountants (NZICA)
- South African Institute of Chartered Accountants (SAICA)

These organisations represent around 775,000 professional accountants in over 165 countries from around the globe.

The GAA was established to promote quality services, share information, and collaborate on important international issues, whilst operating in the interest of a quality accounting profession and the public interest. The over riding objectives of the GAA are those of operating in the interest of a quality accounting profession and the public interest.

In addition the GAA has the objective of:

1. enhancing the accounting profession and business through global leadership in the areas of thought leadership and research.

2. assisting the development of national accounting institutes and their national qualifications

3. promoting the brands represented by the member bodies through their linkages with the GAA, enabling growth for the member organisations.

4. increasing advocacy leverage with national regulators, Governments and stakeholders through member body collaboration, articulation of consensus views and working in collaboration with other international bodies such as IFAC.