Federation of European Accountants
Fédération des Experts comptables Européens

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Submitted through:
http://www.esma.europa.eu/consultation/66722/response

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Dear Ms. Damianov,

Re: FEE responds to ESMA Consultation Paper 'ESMA Guidelines on enforcement of financial information'

(1) FEE (Fédération des Experts-comptables Européens - Federation of European Accountants) is pleased to provide you with its comments on the Consultation Paper 'ESMA Guidelines on enforcement of financial information' (the Guidelines). FEE represents 45 professional institutes of accountants and auditors from 33 European countries, including all of the 28 EU Member States. It has a combined membership of more than 700.000 professional accountants whom, among other things, are responsible for the preparation of financial statements of listed companies or the statutory audit thereof. Therefore, our comments focus on the questions related to the Guidelines that might affect the accounting and auditing profession. We would like to comment on the most relevant matters from our perspective, as set out in the appendix below.

(2) We welcome ESMA's efforts to promote a common European approach to the requirements in the Transparency Directive on the enforcement of financial information and ensure a level playing field across the EU. Hereby ESMA needs to aim at furthering the cooperation of national competent enforcement authorities at the European level, without overstepping the boundaries of the Transparency Directive. It should be noted that ESMA has no legislative powers regarding the enforcement of financial information.

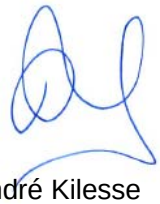
(3) It would be helpful for ESMA to explain why it has used its power under Article 1(3) of the ESMA regulation in this regard. More specifically, stating the reasons why the Guidelines are necessary to ensure the effective and consistent application of the Transparency and Prospectus Directives would be helpful.

(4) Finally, in trying to achieve a common European enforcement approach, it would be very useful for ESMA to measure its effectiveness in promoting a common European enforcement approach when the final Guidelines are being applied by national enforcement authorities.

FEE is highly committed to supporting ESMA in its next steps in finalising the Guidelines.

Please do not hesitate to contact us if you wish to discuss any of the points raised in our response. For further information on this letter, please contact Laura Buijs, Manager - Corporate Reporting, at the FEE Secretariat on +32 2 285 40 71 or via e-mail at laura.buijs@fee.be.

Yours sincerely,



André Kilesse
President

Olivier Boutellis-Taft
Chief Executive

APPENDIX

Q1 Do you think that the proposed guidelines will improve the quality and consistency of financial reporting in Europe?
We welcome ESMA's efforts to promote a common European approach to the requirements in the Transparency Directive on the enforcement of financial information and ensuring a level playing field in Europe.
Q2 Do you have any comments on the potential costs to the financial reporting community of any aspects of these proposals?
No comment.
Q3 Do you agree that a common European approach to the enforcement of financial information is required in order to avoid regulatory arbitrage by issuers? In this context, regulatory arbitrage refers to the position where an issuer's choice of the market on which to list its securities may be influenced by different approaches to enforcement being applied in different European jurisdictions.
First of all, we question if, and if so, to what extent, this regultatory arbitrage is actually happening or will happen. We do not assume that many companies would actually change the location of their registered office or the regulated markets where their securities are listed in order to fall under a different enforcement regime. In case companies do change location, it is most commonly for other reasons, such as the depth of the foreign market and/or gaining access to capital. More importantly, we encourage ESMA to make sure that any issuer of listed securities falls within the enforcement regime of a particular Member State. Member States can choose the scope of their enforcement regime, which usually is determined by the fact that the issuer's registered office is within the Member State, or their securities are listed on the Member State's regulated market. Therefore, an issuer whose registered office and securities listing are located in two different Member States could be subject to two different enforcement regimes. This undesired consequence should be avoided. Finally, we would like to address the need for each Member State to have a competent enforcement body in order for the common European approach to succeed. Only national bodies can take into account the specific requirements in each jurisdiction, such as those related to corporate governance and tax.
Q4 Do you agree with the objective, definition and scope of enforcement set out in paragraphs 11 to 21 of the proposed guidelines?
We welcome that ESMA has extended the objective of enforcement in CESR Standards No. 1, to not only include 'contributing to the investors' decision making process', but, in Guideline 1, also to state the decision making process of 'other users of financial information'. We consider recognising the broader range of stakeholders of financial reporting essential, in order to have enforcement protecting their interest as well.

Q5 Do you agree that issuers from third countries using an equivalent GAAP to IFRS should be subject to an equivalent enforcement and coordination system? Do you agree with the measures proposed to make this enforcement more efficient?
No comment.
Q6 Do you agree that enforcers should have the powers listed in paragraph 30 of the proposed guidelines? Are there additional powers which you believe that enforcers should have?
Guidelines 26 to 29 provide more details on article 24 (1-3) of the Transparency Directive on competent authorities. FEE would like to note that these Guidelines should remain within the realm of the Transparency Directive and not detract from enforcement systems that are currently in place and that are in line with the Transparency Directive. This is important as the Guidelines aim to further the coordination of national competent enforcement authorities at the European level within the boundaries of the Transparency Directive. The Guidelines should not stipulate how the enforcement structures are set up under national law. We would like to point out that both the Transparency Directive article 24 (2) and the Guidelines (paragraph 26) state that the final responsibility for supervising compliance with the provisions of the Transparency Directive remains with the designated central competent authorities of the relevant Member State. Generally speaking, and also in this instance, the Guidelines should not pose any additional requirements to those stated in the Transparency Directive. We agree in principle with the powers as listed in paragraph 30 of the Guidelines which correspond with those in article 24(4) of the Transparency Directive. Regarding the requirement for auditors sub b) in paragraph 30 of the Guidelines and sub a) in article 24(4) of the Transparency Directive, to provide any relevant information and documentation relevant for enforcement, we would like to draw your attention to Article 24 (6) of the Transparency Directive stating that: *The disclosure to competent authorities by the auditors of any fact or decision related to the requests made by the competent authority under paragraph (4)(a) shall not constitute a breach of any restriction on disclosure of information imposed by contract or by any law, regulation or administrative provision and shall not involve such auditors in liability of any kind.* FEE would encourage for the Guidelines to include the information in this article and clarify that contractual/legal or regulatory restrictions (e.g., professional secrecy/confidentiality) or liability issues can prohibit the auditor from disclosing information to regulators. It would be useful for the Guidelines to acknowledge that, in general, auditors are not the principal source of information about a company for regulators. The company's management, or those charged with its governance (like the supervisory board or the audit committee) are the primary source to provide information and documentation relevant for enforcement.

Paragraph 30b states that enforcers shall have the right to require any information relevant for enforcement at least from issuers and their auditors. As both audit and enforcement contribute to the protection of the financial statement users and the promotion of market confidence, involvement of the companies' auditors in the enforcement process is important. However, it is the financial information provided by the company that is subject to enforcement. Therefore, it is primarily up to the company's management to provide the competent enforcement authority with the explanations and any additional information it might need to fulfil its tasks. Direct contact between the competent enforcement authority and the company's auditor would undermine management's responsibilities for financial reporting. As set out in the European Directive on statutory audits of annual accounts and consolidated accounts, the auditor must be independent of the audited company and may not be involved in the audited company's decision-making , i.e. an auditor may not assume the role of management.

In our opinion, companies should be obliged to inform their auditors of any ongoing enforcement activities. Should management need assistance in providing the required information, it might decide to consult the auditor. The auditor should only act in co-operation with the company's management and at their request. Legal confidentiality requirements generally preclude auditors from providing information about their clients to enforcement authorities unless there is an exception in law, or the client specifically consents to such access. We would like to emphasis that in these cases, the information and documentation required from the auditor is limited to matters pertaining to the financial information that have become known during the audit. Audit working papers that the auditor prepared for his or her own use, such as planning memoranda, work plans etc. do not have to be submitted to the enforcement authority unless they relate directly to the financial information of the entity subject to enforcement.

Finally, paragraph 33 provides enforcers with the right to require necessary information irrespective of whether a suspicion exists and also when their quest is not related to the accuracy of the issuer's financial information. FEE considers that this power for enforcers would be too broad. FEE would therefore argue for the Guidelines to require the enforcer to have a suspicion, or at least a well argued substantially documented reason for executing their right in this regard.

Q7 Do you agree that enforcers should have adequate independence from each of government, issuers, auditors, other market participants and regulated markets? Are the safeguards discussed in paragraphs 38 to 41 of the proposed guidelines sufficient to ensure that independence? Should other safeguards be included in the guidelines? Do you agree that market operators should not be delegated enforcement responsibilities

We fully agree with the need for enforcers to be adequately independent from government, issuers, auditors, other market participants and regulated markets. We especially support Guideline 40 stating that government should not be able to change the composition of any decision-making body of the enforcer during the appointment (e.g. mandate) period.

In this regard, we would encourage clarification of the concept of 'market operators', for which paragraph 38 prohibits the delegation of enforcement responsibilities. It would be helpful to know how this relates to the SRO (Self Regulating Organizations). In this regard CESR Standard No.1 explicitly states that they fulfill the independence requirement if the relevant competent administrative authority monitors that the enforcement mechanism follows all the principles of this Standard.

Regarding the requirements for independence stated in paragraph 39, namely that the enforcer should not be unduly influenced either by members of the political system or by issuers and their auditors and that enforcement responsibilities should not be delegated to market operators, we assume that these do not exclude participation of private stakeholders in the enforcement process. This is especially important because of the positive experience within certain European Union jurisdictions to engage financial reporting review panels in this process. These panels have a mixed composition of public and private stakeholders, such as for instance auditors and issuers.

Q8 Are you in favour of enforcers offering pre-clearance? Do you have any comments on the way the pre-clearance process is described and the pre-conditions set in paragraph 42 to 45 are described?

We accept that pre-clearance is a well accepted practice in some Member States and that the Guidelines do not want to change current practice. We are not in favor of pre-clearance for other forms of financial information than prospectuses. Its suitability should be considered on a case by case basis; pre-clearance decisions should certainly not be seen as general interpretations.
Pre-clearance should only be sought in exceptional, well-defined circumstances. In our view, a formal process needs to be established that fulfills inter alia the following conditions:

- any request by a company must be limited to a specific prospectus;
- the company has already developed a proposed prospectus for this specific case (where applicable, in consultation with its auditor)
- the enforcer seeks the views of the company's auditor, and such views are to be considered and discussed within the pre-clearance process.

Q9 Do you agree that in order to ensure investor protection, the measures included as part of a prospectus approval should be supplemented by additional measures of ex-ante enforcement in relation to financial information? If yes, could you please specify the exact nature of ex-ante enforcement that you would expect from enforcers?

In our opinion ex-ante enforcement could either be defined as a pre-clearance process with regard to the preparation of prospectuses, or an enforcement process comparable to current enforcement of financial statements, but carried out before publication. It seems that only the latter is mentioned by ESMA. In this context, as the historical financial statements included in the prospectuses have normally already been subject to statutory audit and ex-post enforcement (financial statements), we understand that ex-ante enforcement would concentrate only on other financial information, e.g. pro-forma financial statements, profit estimates, MD&A.

If additional ex-ante enforcement measures (legally required governmental enforcement processes) with respect to financial information in a prospectus are established, a sufficient time frame for such additional processes will need to be prescribed by law (e.g. six weeks). It should be clear to all market participants that this will lead to longer lead time schedules when entering capital markets. In consequence, the cost of capital of the companies could be significantly increased.

Additionally, we would like to point out that introducing ex-ante enforcement of prospectuses will necessitate an increased number of high qualified staff within the national competent enforcement authorities.

Q10 Do you agree that a risk-based approach to selection should not be used as the only approach as this could mean that the accounts of some issuers would potentially never be selected for review?
No comment.
Q11 Do you agree that the risk-based approach should take into account both the risk of an individual misstatement and the impact of the misstatement on financial markets as a whole?
No comment.
Q12 Do you think that a maximum period should be set over which all issuers should have been subject to at least one full review (or to be used to determine the number of companies to be selected in sampling)?
No comment.
Q13 What are your views with respect to the best way to take into account the common enforcement priorities established by European enforcers as part of the enforcement process?
The identification of common enforcement priorities is an important aspect in furthering the coordination of European enforcement activities. With regard to ESMA and national enforcers establishing common enforcement priorities, we believe that these should leave sufficient flexibility for the national competent enforcement authorities to add domestic priorities, taking into account their specific circumstances.
Q14 Do you agree that the examination procedures listed in paragraph 54 of the proposed guidelines are appropriate for an enforcer to consider using? Are there other procedures which you believe should be included in the list?
Guideline 8 states that as part of the ex-post enforcement activities, enforcers can either use full reviews or a combination of full reviews and partial reviews of financial information. In this respect we do not share the view expressed by ESMA that carrying out only partial reviews would not be fit for enforcement purposes. The choice between full or partial review should be based on a case-by-case assessment taking into account enforcement priorities, a defined risk approach and resources utilisation. We believe that in practice, there are instance where a full review may not provide added value compared to a partial review and therefore the enforcer's resources would not be usefully spent on a full review. Furthermore, a systematic "full review" might create expectations that not all enforcement authority could usefully and economically meet. ESMA should limit administrative burden to what is necessary and proportionate for both enforcement authorities and issuers. It should also be clarified that a review by an enforcement authority is not aimed at second guessing the audit.
Q15 Do you agree that, in determining materiality for enforcement purposes, materiality should be assessed according to the relevant reporting framework, e.g. IFRS?
The concept of materiality is crucial to financial reporting. We support ESMA's view that improvement is needed in this area. However, the responsibility for determining this should remain with the IASB. Therefore, we welcome the announcement of the International Accounting Standards Board to start a project on materiality in the context of revising International Accounting Standard (IAS) 1, *Presentation of Financial Statements*.

Q16 What are your comments regarding enforcement actions as presented in paragraphs 57 to 67 of the proposed guidelines? Do you agree with the criteria proposed?
In our opinion, the three enforcement actions listed in paragraph 57 and the criteria for deciding which action is required to be taken are suitable. Considering the objective of enforcement stated in Guideline 1, we would welcome clarification that no further enforcement action needs to be taken if the issuer has corrected a misstatement by means of a restatement, a corrective note or a correction in its future financial statements, thereby ensuring that investors and other users were well-informed on a timely basis. We recognise the sensitivity of the issue of material misstatements. We acknowledge that this issue can be viewed from both the market participants' perspective as well as the angle of financial reporting. Regarding paragraph 58 and 59 which consider immaterial departures from the financial reporting framework, we, from a financial reporting perspective, wonder why 'immaterial departures that are left intentionally uncorrected' would not remain considered as immaterial and thus not require correction. The same goes for 'immaterial departures that are at a significant risk for becoming material in future'. We are of the view that immaterial departures from the financial reporting framework, independent of their nature or cause, should remain considered as immaterial and thus not require correction as required by the enforcer. Additionally, we suggest the section on European coordination (paragraphs 68 to 73) also stipulate that the decisions on which action is required to be taken should be a matter for coordination among European enforcers
Q17 Do you have any comments on the specific criteria for the submission of decisions or emerging issues to the EECS database?
Regarding the specific criteria for submission of emerging accounting issues (ex-ante) to the EECS database, we find that the criterion of 'significant importance for the European regulated markets' is crucial. This should not be an alternative criterion, but it should always be fulfilled together with one or more of the three other criteria proposed in Guideline 14 before an accounting issue needs to be submitted as an emerging issue. We agree with the specific criteria for the submission of decisions (ex-post) to the EECS database. Additionally, we would like to suggest establishing a database such as EECS at the global level. Regarding the ESMA Statements and/or Opinions mentioned in Guideline 13, FEE finds that these can help in the ongoing dialogue between ESMA and the profession. ESMA, in coordinating the national enforcement authorities, can use Statements and/or Opinions to explain the concepts underpinning their enforcement and the methods they use in their operations. A good example of this is the ESMA Public Statement on Sovereign Debt in IFRS Financial Statements. Notwithstanding our support of Guideline 13 as explained above, we would like to add our strong support for paragraphs 72 and 73 precluding ESMA from issuing IFRS application guidance, as the IFRS Interpretations Committee remains the sole source of interpretation of IFRSs.

Q18 What are in your opinion appropriate activities that would help to achieve a high level of harmonisation of the enforcement in Europe?
We strongly encourage for all Member States' enforcement authorities to participate in EECS. It would be a big step forward if all national authorities would disclose their areas of focus and summaries of their findings and recommendations.
Q19 Do you have any comments on the transparency, timing and frequency of the reporting done by the enforcers with respect to enforcement actions taken against issuers?
We agree with ESMA that the publication of enforcement actions taken against issuers on an anonymous basis in the EECS Database of Enforcement could provide helpful advice to all issuers and facilitate the exchange of information and expertise. However, we think that enforcement authorities should be cautious so as not to assume a standard setting role by issuing reports that contain statements on specific accounting treatments (we also refer to our comment on question 17). Furthermore we would like to propose that the content of the periodic reports on enforcements activities from the national enforcement authorities should also be subject to European coordination in order to avoid perceived differences in the strength of enforcement between the European Member States.
Q20 What are your views about making public on an anonymous basis enforcement actions taken against issuers?
No comment.