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Dear Dr Dermody,

I have had a while to reflect on some of the issues I was asked about during the committee hearing on April 14 and one matter I have not previously added observations regarding is the deadline for the adoption of international financial reporting standards. I hope the brief remarks that appear below assist the committee in thinking about the issues underlying some of the remarks I made in response to a question from Senator Andrew Murray during the latter part of session. On reading the transcript there was also an aspect of a question I was asked by Senator Stephen Conroy that I failed to answer completely relating to the future of the Urgent Issues Group. I answer that aspect of his final question to me in the latter part of this correspondence.

One of the points I failed to expand on during that portion of the hearing is the fact that the deadline for the adoption of International Financial Reporting Standards – the January 2005 deadline – has been a target various companies have been trying to meet for some time. I am aware as a result of conversations with accountants working in listed companies that they have been concerned about the potential for deferral because their project planning hinged on the deadline staying fixed. Speculation about a delay merely threw their planning into doubt and also created some degree of procrastination on the part of their own staff in relation to progressing with aspects of their implementation projects. This has been evident given the conversations I have had with corporate accountants that have attended conferences I have spoken at over the past two years and contacted me via e-mail or by phone.

Much has been said about French recalcitrance<sup>1</sup> on fair valuation of financial instruments and the move to force insurers to account on a consistent basis in Europe. That – meaning the childlike burbling from Europe on some accounting standards - has

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<sup>1</sup> The most recent information I have is that the European Financial Reporting Advisory Group (EFRAG) has approved the contentious standards on financial instruments for endorsement along with the other recently issued standards such as the ones on insurance contracts and business combinations. While there is some opposition left it is, according to the most recent reports, gradually subsiding. The European endorsement process has still got to go through the political process. It is expected to occur a little later this year.



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been used by some commentators as an argument for deferring Australian adoption of international standards. That argument – in my view – only holds any validity if by some strange twist of fate Australia is proven to be a member of the European Union and is somehow bound by the resolutions of the European Parliament on the adoption of IFRS. The last time I checked Australia was not a member of the European Union and there is nothing that binds us to any legislative edict that emerges from the European continent. Sheer logic should lead us to the conclusion that there is little to stop us from adopting what is there as at March 31, 2004 and then taking a stand on the amendments that flow on afterwards by delaying their implementation in the Australian context. That is the way for this country to exercise its power and what influence it has in the international playing field at the current time. Had Australia initially set a different deadline that had no linkage to the European situation that argument would be unavailable to those intellectually dishonest enough to parade it as a legitimate reason to delay the introduction of various standards that will improve aspects of accounting in Australia.

Most of the gaps that exist in Australian accounting standards were a result of the Australian standard setters failing to act back in the early 1990s to introduce specific standards on accounting for intangible assets, defined benefit super funds and financial instruments. What you have gradually seen is that the International Accounting Standards Board has advanced within a shorter timeframe areas of accounting past generations of standard setters failed to deliver outcomes in Australia. The period in the early 1990s was the period when Australia was capable of doing serious original work in accounting thought. Much of what was done in the latter part of the 1990s was the incorporation of other people's work in the domestic accounting framework. Originality was limited two key areas: accounting for life insurance, which is possibly the only area where the domestic market has a case to maintain existing Australian accounting treatments<sup>2</sup>, and accounting for what are known as self-generating and regenerating assets. The latter two standards were of leadership quality and SGARA standard was used as a template for the international standard that was subsequently developed on the matter. Most of the other standards constituted in large part a 'download' of the literature of the then International Accounting Standards Committee with some alteration for Australian conditions such as the removal of optional accounting treatments where the AASB deemed necessary. The situation the board, which was led by the late Ken Spencer at the time, nurtured was one where companies complying with Australian standards could generally claim to be complying with international standards. A foreign company listed on the Australian Stock

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<sup>2</sup> We can keep the Australian insurance standards with some amendments by arguing the international accounting standard setter does not have a comprehensive set of standards dealing with insurance. I understand the AASB intends to pursue that strategy.



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Exchange could, for example, lodge financial statements that comply with international standards, but those financial statements would not be in line with the Australian standards of the day. This is because the AASB's policy of excising options from international accounting standards would mean a foreign company listed on the stock exchange could conceivably use an option in the international standards that was not the accounting treatment blessed and included in the Aussie standard by the Australian standard setter. The current environment is very different to that of the past insofar as the goal is the attainment of a single set of standards in as quick a possible time. Change – particularly a great amount of change in a short frame of time – means there will be growing pains to a high degree. That is what we are presently seeing in many parts of the community grappling with the issue of moving to international accounting standards.

This brings me to the debate some people have concerning the quality of accounting standards. If one takes the approach that the attainment of a single set of global reporting standards is the first and most critical objective then a debate on the quality of individual components is irrelevant. Once a single platform has been achieved then improvements to the framework of reporting can be incremental. If a debate on the quality of the individual standards making up the international accounting standards jigsaw puzzle then we will be here until the end of the current millennium arguing the merits and demerits of individual accounting treatments without any advancement in the move to get to a single reporting platform across the globe. The committee should place on the table those two questions in its consideration of the issues related to the adoption of international accounting and, indeed, international auditing standards.

Senator Conroy asked me during a discussion on aspects of the standard setting system as to what I believed was the future of parts of it. I answered the question fairly generically, but there was a certain part of the question I failed to deal with in any comprehensive sense. I outlined what I thought should be the plans for the future of the Australian Accounting Standards Board, but failed to address the future role of the Urgent Issues Group in the Australian environment when aspects of the interpretation of standards is done by the International Financial Reporting Issues Committee, which is the global interpretations body that is effectively the subcommittee of the International Accounting Standards Board. The UIG's future will be significantly dependent on domestic accounting firms, companies and public sector authorities bringing issues to it for resolution. The IFRIC will be unable to resolve every problem of an accounting nature that crops up in this market so the need for the UIG will still be there. It may meet for fewer times each year or it could even meet in conjunction with the AASB in order to resolve interpretational issues. It should also be used by the AASB as a sounding board



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for submissions being put forward to the IASB on international exposure drafts that will eventually make their way into the law by virtue of our giving the accounting pronouncements legal force in the way we do here in Australia. There is an additional problem on matters of interpretation that involves the Financial Reporting Panel. A case before the FRP may create a persuasive precedent that companies will follow that may not necessarily be in line with the international standards. This could occur if the panel members hearing a case decide a specific set of facts fits a particular kind of accounting without necessarily appreciating potential subtleties in the interpretation of the standards. Interpreting the standards in the context of the disputes between the Australian Securities and Investments Commission and a company could result in the establishment of general reporting practices that are inconsistent with the way international standards might be dealt with in other jurisdictions. That is something to also bear in mind.

I hope this helps the committee in its deliberations as it moves closer to finalising its inquiry into CLERP 9. I would be pleased to explore these matters further with committee members and the committee secretariat should there be any further inquiries.

Kind Regards

Tom Ravlic SIA (aff)