



European Securities and
Markets Authority

Report

Activity Report of the IFRS Enforcement activities in Europe in 2012



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Annex I: List of European Enforcers

List of abbreviations and acronyms used in this report:

| | |
|------------------------|---|
| CA | Competent Authority |
| CESR | Committee of European Securities Regulators |
| CRSC | Corporate Reporting Standing Committee |
| EEA | European Economic Area |
| EECS | European Enforcers Coordination Sessions |
| EU | European Union |
| IASB | International Accounting Standards Board |
| IFRS | International Financial Reporting Standards |
| IFRS IC | International Financial Reporting Standards Interpretation Committee |
| US SEC | United States Securities Exchanges Commission |
| ESMA Regulation | Regulation 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC |
| IFRS Regulation | Regulation (EC) No 1606/2002 of 19 July 2002 of the European Parliament and of the Council on the application of international accounting standards |
| Transparency Directive | Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market |

Executive Summary

This report provides an overview of the monitoring of compliance of financial information with International Financial Reporting Standards (IFRS) and the taking of appropriate enforcement actions in the European Economic Area (EEA) in the year ended 31 December 2012. The report is based on the activities of the European Securities and Markets Authority (ESMA) and accounting enforcers in the EEA (European enforcers). The main objective of ESMA's European Enforcers Coordination Sessions (EECS) is to co-ordinate the enforcement activities in the EEA countries in order to increase convergence amongst European enforcers' activities and contribute to fostering investor confidence.

The report provides a description of the existing enforcement system in Europe, the main activities that were coordinated at European level during 2012, ESMA's cooperation with the international standard setter and third country enforcers on matters related to IFRS, and provides quantitative data on enforcement activities.

Enforcement activities in 2012 continued to focus on the effects of the financial and economic crisis. As a follow-up of the ESMA Statements and Opinion issued in 2011 in relation to exposure to Greek Government bonds, ESMA published a report on the review of accounting practices relating to the adequate recognition and measurement of impairments resulting from exposures to Greek Government bonds in the 2011 annual IFRS financial statements. Identification of additional impact of the financial and economic crisis on financial institutions' activities continued to be an important area monitored at European level and ESMA published a public statement on forbearance activities stressing the need for consistent application of the IFRS requirements relating to the impairment of financial assets modified due to financial difficulties of the borrower.

As a result of the poor economic outlook, there was a presumption that assets in many industries may generate lower cash-flows. ESMA undertook a review over more than 200 issuers with significant amounts of goodwill and found out that impairment of goodwill was limited to a handful of issuers and that in many cases disclosures related to key assumptions or sensitivity analyses were not entity-specific and thus not useful for investor decision making purposes.

EECS activities have been intensified to bring more coordination and consistency of enforcement activities in Europe. In 2012, for the first time, ESMA together with European national enforcers identified and made public common enforcement priorities on financial reporting topics which were identified as particularly significant for European issuers for the preparation of the 2012 IFRS year-end financial statements.

IFRS enforcement activities at Member States' level have increased in 2012 compared to the previous year and European enforcers reviewed more than 2 000 interim or annual IFRS financial statements and took around 500 enforcement actions. The conclusions of the enforcement activities shows that overall the quality of the IFRS financial statements continued to improve as a result of the significant experience gained by the preparers with

IFRS application since the first time application in 2005. Nevertheless it was noted that there is still room for improvement in the quality of financial reporting in certain areas. Examples of areas requiring additional effort from issuers in order to comply with IFRS include: application of the classification criteria for assets held for sale, determination of the discount rate for the calculation of defined benefit obligations, classification and measurement of financial instruments, assessment of goodwill impairment, distinction between a change in an accounting policy and an accounting estimate and disclosures about the risks and uncertainties or judgments and estimates used in preparation of IFRS financial statements.

ESMA together with the national competent authorities will reinforce the level of convergence of financial information supervision and enforcement activities reflecting the strong commitment to contribute to the consistent application of IFRS around the globe.

I INTRODUCTION

1. This report provides an overview of the financial information supervision and enforcement activities carried out during the year ended 31 December 2012 at European and national levels in the European Union and those countries from the European Economic Area (Iceland and Norway) who agreed to comply with the Transparency Directive and IFRS Regulation. They are generally referred to as “European” activities in the content of the report.
2. The report is addressed to all market participants including European issuers, investors, auditors, other regulators and the general public. It focuses only on enforcement activities related to IFRS financial statements and does not take into account any other supervision activities done by national enforcers on other general accounting practices.
3. In the following sections, the report describes the existing enforcement system in Europe and the main activities coordinated at European level during 2012; it provides quantitative data on enforcement activities in European jurisdictions and describes ESMA’s cooperation with other third parties on matters related to IFRS.

II DESCRIPTION OF THE ENFORCEMENT SYSTEM

4. This section provides a description of the main features of the European enforcement system on financial reporting. Enforcement activity refers to the monitoring of compliance of financial information with the applicable reporting framework and taking appropriate measures in respect of infringements discovered in the course of compliance reviews.

European enforcement system on financial reporting

5. ESMA was set up with the objective of helping foster supervisory convergence in Europe and thereby reducing regulatory arbitrage resulting from different supervisory practices. Divergent enforcement practices could undermine not only the integrity, efficiency and orderly functioning of markets but also have an impact on financial stability. One of ESMA’s areas of responsibility is to promote the effective and consistent application of the European Securities and Markets legislation with respect to financial reporting.
6. The scope of enforcement of financial information of listed companies on the regulated markets as defined under the Transparency Directive covers all reporting frameworks that might be applicable to listed issuers including: IFRS for consolidated financial statements, national GAAPs when applied to non-consolidated financial statements and third-country accounting standards for non-European issuers, if deemed equivalent to IFRS or IFRS as endorsed in the EU. However, the main areas of focus of ESMA are in relation to issues derived from the requirements in the Transparency Directive in relation to the application of the IFRS Regulation.

7. Convergence amongst enforcers on technical decisions taken when reviewing IFRS financial statements is key to the EU Single Market. To meet this objective, ESMA put in place EECS, a forum of 37 European enforcers from the 27 Member States and the two countries in the European Economic Area who have responsibilities in the area of supervision and enforcement of financial information. With more than 6000 listed issuers publishing IFRS financial statements on the European regulated markets, EECS currently constitutes the largest enforcers' network with supervision responsibilities in IFRS globally.
8. Through EECS, European enforcers are able to share and compare their practical experiences on the enforcement of IFRS financial information provided by companies who have, or who are in the process of having, securities admitted to trading on a regulated market in Europe. It provides a forum to discuss enforcement cases before or after decisions are taken by the European enforcers. As a forum of technical experts, this group provides technical advice on issuance of ESMA Statements and/or opinions on accounting matters which deserve specific focus. In addition, it reviews accounting practices applied by European issuers to enable ESMA to monitor market developments and changes in those practices.
9. As a result of the enforcement coordination, ESMA is able to identify areas where a lack of guidance from the standards or divergent interpretations of the IFRS are observed. Such matters are then referred to the IASB or the IFRS IC, as appropriate.
10. Based on the requirements in the Transparency Directive, in 2003 and 2004, ESMA (at that time, CESR) established a framework for the enforcement activity by issuing two principles based standards: Standard No. 1 – Enforcement of standards on financial information in Europe (CESR/03-073¹) and Standard No. 2 – Co-ordination of enforcement activities (CESR/03-317c²), accompanied by Guidance for implementation of co-ordination of enforcement of financial information (CESR/04-257b³). Those standards constitute the basis for the convergence of supervisory practices on financial information in the EU.
11. ESMA has started the review of the standards previously issued by CESR in order to take into account the experience gained from their use and the new legislative framework under which ESMA operates. A preparatory fact-finding phase with the objective of better understanding the characteristics of the existing European enforcement organisation was finalised in 2011. Its outcome has been used by ESMA to identify possible improvements to the IFRS enforcement organisation and constitutes the basis for issuing ESMA guidelines on enforcement.
12. The proposed draft guidelines, which will be subject to public consultation in 2013, contain elements that national enforcers must make every effort to comply with as part of their enforcement process. The draft guidelines define the enforcement and its scope, common

¹<http://www.esma.europa.eu/popup2.php?id=192>

²<http://www.esma.europa.eu/popup2.php?id=2046>

³<http://www.esma.europa.eu/popup2.php?id=2557>

characteristics of the enforcers, specific elements of the enforcement activities (such as selection methods, enforcement actions) and coordination practices at European level.

Enforcement system at national level

13. Supervision of listed entities and enforcement of financial information is performed at national level as required by the Transparency Directive, according to which each Member State has to designate a Competent Authority for the enforcement of financial information.
14. In most countries enforcement is carried out by one authority. In the United Kingdom and Ireland two authorities are involved: one authority deals with periodic financial reports and the other with financial information in prospectuses. In Denmark there is one authority which deals with financial information in prospectuses as well as periodic financial information of financial entities and one authority which deals with periodic financial reporting by non-financial entities. Portugal has a similar system in which one authority is in charge with the enforcement of financial information of all issuers, but shares those responsibilities with the prudential supervisors for the financial institutions and insurance companies.
15. According to the Transparency Directive, other organisations are allowed to carry out enforcement activities, either in their own right or on behalf of the competent administrative authorities, provided that these bodies are supervised by, and responsible to, the relevant competent administrative authority. Only Germany and Sweden make use of that option to delegate part of the enforcement activity from the competent authority.
16. On 5 December 2012, the Austrian Parliament passed a law that led to the establishment of an enforcement process regarding the financial reporting of companies with securities traded on a regulated market, which applies from 2013. Austria will implement a two-tier enforcement system delegating part of the enforcement activity from the competent authority to a review panel. Austria was the last country in the European Union that did not have a formal IFRS enforcement process.
17. Irrespective of the different structures adopted by national enforcers, which can lead to different processes and scope of activity, all national enforcers serve a single and common objective – to promote market confidence and protect investors by contributing to the transparency of financial information via the effective and consistent application of the reporting standards.

III OVERVIEW OF ACTIVITIES COORDINATED IN EUROPE

18. This section provides an overview of the main activities coordinated by ESMA in 2012:

- A. European enforcers reviews of IFRS accounting practices
- B. Common enforcement priorities for the 2012 year-end IFRS financial statements
- C. Issuance of ESMA Statements and/or opinions
- D. Coordination of enforcement decisions
- E. ESMA enforcement database
- F. Other activities

A) European enforcers reviews of IFRS accounting practices

19. Analysis and comparison of accounting practices applied by IFRS issuers allows ESMA to identify trends developing in relation to a specific standard, in certain industries or jurisdictions. ESMA chooses to perform reviews when specific market developments or changes in accounting practices occur or as a follow-up of previous studies.
20. Such reviews require the creation of dedicated project teams consisting of national experts from European enforcers and ESMA staff. Their work is generally based on publicly available information.

Accounting practices related to exposure to sovereign bonds

21. The financial crisis had a major impact on the financial position and performance of publicly traded companies. As a result of the developments in the sovereign debt markets and due to an increased need for transparency to investors, ESMA performed a very detailed analysis of the accounting practices of European financial institutions with respect to their exposure to sovereign debt.
22. In 2012, ESMA together with the enforcers, engaged in a review of the accounting practices in the 2011 annual IFRS financial statements in relation to the recognition, measurement and disclosure of impairments in relation to Greek Government bonds. These matters have been previously stressed in the ESMA's Statement and Opinion issued in 2011 (ESMA/2011/226⁴ and ESMA/2011/397⁵) that discussed the IFRS requirements in relation to the above mentioned matters.

⁴http://www.esma.europa.eu/system/files/2011_226.pdf

⁵http://www.esma.europa.eu/system/files/2011_397.pdf

23. The review covered around 50 financial institutions from 14 jurisdictions with a total gross exposure of around EUR 80 billion as at 31 December 2011. The report (ESMA/2012/482⁶) noted that enforcers observed a good level of consistency as regards the level of impairment losses recognised in the 2011 annual financial statements. The report also highlighted key areas where disclosures could have been improved mainly in relation to: transparency about gross exposures, bonds maturities, changes in the level of exposure over the reporting period and exposure to credit default swaps.

Reporting practices in relation to impairment of goodwill and other intangible assets with indefinite useful lives

24. As reported in the 2011 and 2010 ESMA's activity reports on IFRS enforcement, the application of IAS 36 had been identified as one of the areas posing challenges to issuers taking into account the low quality of disclosures provided in the financial statements. Taking into account the effects of the financial and economic crisis and given the poor economic outlook in various areas, concerns arose as to the way issuers apply the requirements in IAS 36 when assessing the need for impairment of assets.
25. In 2012, ESMA together with the European enforcers performed a review of the IFRS financial statements of more than 200 listed issuers from 23 European jurisdictions with total goodwill amounting to around EUR 800 billion as of 31 December 2011. The report (ESMA/2013/2⁷) illustrates that goodwill impairment losses recognised in 2011 were limited to a handful of issuers and concentrated in a very limited number of industries (mainly telecom and financial services). Although a decrease in market capitalisation may not lead directly to impairment, the increased equity/market capitalisation ratio can call into question whether the level of impairment in 2011 reflects the effects of the financial and economic crisis appropriately.
26. Enforcers also noted that, although the major disclosures related to goodwill impairment testing were generally provided, in many cases these were of a boiler-plate nature and not sufficiently entity-specific. In particular, the description of key assumptions used by management, explanations on how growth and discount rates used in impairment tests were determined, and the sensitivity of the test results to reasonable possible changes in key assumptions were not sufficiently well described. This means that, in many cases, the users of the financial statements are not able to evaluate the reliability of the assumptions used from the disclosures given, which is the primary purpose of those disclosures.
27. As a consequence, ESMA and European enforcers decided to monitor this area in 2013 and included this topic in the common enforcement priorities defined for the 2012 annual financial statements. The review will aim at improving the rigour applied by issuers in the impairment test of goodwill, monitoring the application and compliance of IFRS requirements on goodwill impairment in particular with regard to the areas mentioned above and assess whether sufficient relevant disclosures are provided by the issuers.

⁶<http://www.esma.europa.eu/system/files/2012-482.pdf>

⁷<http://www.esma.europa.eu/system/files/2013-02.pdf>

Consultation Paper on considerations of materiality in financial reporting

28. A recurring theme arising in the coordination of IFRS enforcement relates to the apparently differing views regarding the practical application of the concept of materiality amongst issuers, auditors, possible users of the financial reports and, in some instances, accounting enforcers. ESMA published a Consultation Paper in 2011 (ESMA/2011/373⁸) considering the role and implication of materiality in financial reporting. In 2012, ESMA published the summary of the 50 responses received (ESMA/2012/525⁹) and organised a public roundtable to discuss topics where further clarification was needed.
29. Consistent with the results of the consultation, ESMA does not plan to publish any guidance on materiality, but will continue to engage with the IASB and the International Auditing and Assurance Standards Board (IAASB) in respect of key messages arising from the consultation process and provide both relevant enforcement examples where consistent application of materiality was found to be problematic and relevant input for the project started by the IASB on the Disclosure framework. ESMA also published a feedback statement in February 2013 (2013/218¹⁰).

B) Common enforcement priorities for the 2012 year-end IFRS financial statements

30. An important step in ensuring coordination at European level consists in informing stakeholders (issuers, auditors and enforcers) on important accounting matters that are relevant for the following reporting period prior to the finalisation of the financial statements.
31. In order to promote consistent application of IFRS, ESMA together with European enforcers, identified common enforcement priorities in advance of publication of issuer's 2012 IFRS financial statements. As a consequence, an ESMA technical alert was published in November 2012. The Statement (ESMA/2012/725¹¹) contains financial reporting topics that were identified as particularly significant for European issuers on the basis of relevant economic and market situations observed in 2012.
32. These priorities focused on the following topics:
 - financial instruments and, in particular, the need for relevant disclosures on financial instruments subject to risk, sovereign debt exposures and impairment of financial assets;

⁸http://www.esma.europa.eu/system/files/2011_373_.pdf

⁹http://www.esma.europa.eu/system/files/2012_525.pdf

¹⁰<http://www.esma.europa.eu/system/files/2013-218.pdf>

¹¹<http://www.esma.europa.eu/system/files/2012-725.pdf>

- recognition, measurement and disclosures of impairment of non-financial assets, and, in particular, goodwill;
- measurement of defined benefit obligations, with a focus on the determination of the discount rate and the new provisions of IAS 19; and
- recognition of provisions for non-financial liabilities.

33. Monitoring how issuers address these priorities is part of the work programme of European enforcers, who will consider them in their review of financial statements for the year ended 31 December 2012. ESMA will report in 2013 how European issuers applied the IFRS requirements in relation to these topics based on information reported by each jurisdiction.

C) Issuance of ESMA Statements and /or opinions

34. As part of EECS discussions, some issues may refer to cases which are of significant importance to the European regulated market. This was the case in 2012 in relation to accounting for forbearance practices for which it was decided to issue a public statement.
35. As the financial crisis had a major impact on the financial position and performance of publicly traded companies in the financial sector, concerns arose as to the lack of transparency regarding forbearance-related practices, the amounts at stake, and the potential impact this might have on issuers' financial performance and consequently for investors and markets.
36. Following a limited fact-finding exercise carried out on a sample of financial institutions, ESMA noted that disclosures about forbearance practices in the financial statements diverged significantly and were often limited in the amount of information provided and vague as to content. In some cases it was unclear whether forbearance measures were considered objective evidence of impairment and whether, and to what extent, the need for forbearance led to recognition of impairment losses.
37. Consequently, ESMA published in December 2012 the Statement on Forbearance Practices in the IFRS Financial Statements (ESMA/2012/85312) in order to contribute to the accuracy, transparency and comparability of IFRS reporting in relation to that matter. The public statement included a definition of forbearance¹³, based on the application of the requirements included in IAS 39 – *Financial Instruments: Recognition and Measurement*. It underlined that this practice constitutes objective evidence of impairment and indicated the accounting treatment and disclosures IFRS require in these circumstances. In particular, ESMA asked for application of a heightened level of scepticism when assessing impairment of loans subject to forbearance and stressed the importance of providing

¹²<http://www.esma.europa.eu/system/files/2012-853.pdf>

¹³Forbearance – modification of the terms and conditions of the contract due to financial difficulties of the borrower

relevant explanations that would enable users to evaluate the significance of financial instruments and the nature and extent of risks to which an issuer is exposed.

38. This public statement forms part of broader work on forbearance practices undertaken by regulators, including the European Banking Authority (EBA) and the European Systemic Risk Board (ESRB), who are examining the issue in the context of prudential reporting and macro-economic risks respectively.
39. Monitoring the level of transparency provided by financial institutions through both qualitative and quantitative disclosures on forbearance practices in the 2012 IFRS financial statements constitutes an important area for ESMA and European enforcers. Future cooperation between ESMA, EBA and ESRB is envisaged on this topic, and also on other financial reporting matters of concern for financial institutions.

D) Coordination of enforcement decisions

40. A key part of ESMA's coordination role lies in analysing and discussing emerging issues and decisions taken by European enforcers in respect of financial statements published by issuers with securities traded on a regulated market and who prepare their financial statements in accordance with IFRS.
41. ESMA and European enforcers met eight times during 2012, with a significant part of their meetings being dedicated to the discussion of accounting issues submitted by national enforcers. In addition, special meetings were held by ad-hoc working groups on issues which are described in other sections of this report.
42. The emerging issues may refer to cases which are of relevance to other European issuers, are of significant importance to the European regulated markets or have been identified as being widespread. This was the case in 2012 when following up how prior ESMA statements and opinion on sovereign bonds have been taken into account by market participants and accounting for forbearance practices for which ESMA decided to issue a public statements as previously explained.
43. Other emerging issues deal with a variety of situations where enforcers seek guidance and insight from fellow enforcers prior to taking a decision. The discussion at EECS offers an opportunity to benefit from the experience of other enforcers who have already encountered similar issues, and to discuss the analysis of the technical issue. When time constraints do not allow waiting until the next EECS meeting, emerging issues are discussed during ad hoc conference call or via emails.
44. ESMA has gained an overview of how IFRSs are applied and the main topics which still pose challenges to IFRS issuers from discussions on emerging issues and decisions. While issuers of financial information have developed significant experience in IFRS accounting

over the eight years since the first application of IFRS, ESMA found that there is still room for improvement in the quality of issuers' financial reporting in certain areas.

45. The examples presented below reflect those matters that featured more commonly in decisions brought to EECS for discussion and where relatively more infringements were detected and required corrective action. They also reflect subjects which were more contentious and where value is seen in sharing experience and regulatory responses.
46. Discussion at ESMA was intended to raise the level of consistent application and enforcement of the standards subject to the specific facts and circumstances pertaining to the decisions under discussion. These examples are not intended to represent all types of issues discussed nor all areas where application of IFRS had been challenged by European enforcers; they are merely illustrative of some of the questions most frequently raised.
47. *Presentation of Financial Statements -Going concern*: According to IAS 1 - *Presentation of Financial Statements*, an entity shall prepare the financial statements on a going concern basis unless its management intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. In practice, it seems to be difficult to assess at which point in time it might be considered that there is no more realistic alternative to liquidate. If the going concern basis is no longer appropriate, an alternative basis of preparation of the financial statements has to be used and disclosed.
48. *Non-current assets held for sale and discontinued operations*: Incorrect application of the requirements in IFRS 5 – *Non-current Assets Held for Sale and Discontinued Operations*, was identified with respect to matters such as: inappropriate classification of assets as held for sale beyond the initial period of 12 months, inappropriate allocation of impairment losses to elements included in the group of assets held for sale, and allocation of provisions related to activities to be divested as part of continued activities. In addition, the application of IFRS 5 requirements was discussed in conjunction with a planned initial public offering of a subsidiary and when the means of disposal were modified from an initial public offering to a distribution to shareholders as a dividend-in-kind.
49. *Determination of the discount rate for the calculation of defined benefits obligations*: Due to credit rating downgrades in 2012, the number of high quality corporate bonds which can be used as a reference for assessing the discount rate according to IAS 19 – *Employee benefits* decreased significantly. As a result, questions arose as to which categories of corporate bonds can be deemed “high quality” when debt markets are stressed. This issue was submitted to the IFRS IC, and ESMA monitored the way enforcers addressed this topic in their respective jurisdictions. ESMA and the European enforcers will monitor this topic in 2013 as one of the European Common Enforcement Priorities for 2012 year-end accounts.
50. *Distinction between a change in an accounting estimate and a change in an accounting policy*: This distinction is particularly important because of the differing impact resulting from prospective or retrospective application of the respective changes. Moreover, in

accordance with IAS 8 – *Accounting Policies, Changes in Accounting Estimates and Errors*, in order to change an accounting policy an issuer should be able to justify that the change provides more relevant information, whereas there is no such requirement for a change in accounting estimate.

51. *Disclosures on risks and uncertainties*: Issuers have continued to face risks to their businesses as a result of the continuing generally unfavourable economic climate. In this context, disclosures about risks and uncertainties, or judgements and estimates, used in the preparation of the financial statements are particularly important. Their presentation is often required in the notes due to requirements of IAS 1 or IFRS 7 – *Financial Instruments: Disclosures*, for instance. Due, however, to the use of boiler-plate disclosures that do not accurately describe the facts specific to the issuer and/or transaction, issuers often fail to provide sufficiently tailored information.
52. By stressing the disclosure requirements in the standards, enforcers required disclosures that are material for understanding of the financial position and performance of the issuers and underlined the need to provide disclosures that are entity specific and not boiler-plate.

E) ESMA enforcement database

53. To facilitate the sharing of enforcement decisions and experiences, ESMA established in 2005 an internal database to which European enforcers submit some of the decisions they have taken as part of their national enforcement processes, according to established submission criteria. The criteria are set out in full in the “Guidance for implementation of co-ordination of enforcement of financial information”¹⁴ and include amongst others: material misstatement, complexity of facts and circumstances and potential to conflict with other decisions taken by European enforcers. In order to achieve consistent enforcement decisions throughout Europe, European enforcers consult the database before taking an enforcement decision.
54. As of 31 December 2012, around 250 emerging issues and more than 600 decisions had been entered into the EECS database, out of which 50 emerging issues and 100 decisions have been submitted in 2012. All emerging issues and the most complex decisions were analysed and discussed in meetings held during the year.
55. ESMA regularly publishes enforcement decisions to contribute to the promotion of market confidence and convergence of the application of IFRS. As of 31 December 2012, 139 decisions have been included in a total of 12 publications, with one published in 2012 (ESMA/2012/656¹⁵). ESMA plans to issue further publications regularly. Published decisions are also communicated and included also in the IOSCO database.

¹⁴http://www.esma.europa.eu/system/files/04_257.pdf

¹⁵<http://www.esma.europa.eu/system/files/2012-656.pdf>

F) Other activities

56. In addition to discussing decisions and emerging issues, ESMA provides European enforcers with the opportunity to discuss other matters relevant to their enforcement activities and to develop a better understanding of processes and procedures within enforcement authorities across Europe through reviews or working groups.
57. EECS also provides enforcers with the means of sharing their national publications with fellow enforcers – e.g. enforcers' Activity Reports and other announcements to national markets on issues relating to the monitoring of IFRS. These papers are often presented during EECS meetings.
58. In order to promote a common supervisory culture, educational sessions in relation to newly issued standards issued by the IASB and endorsed in the European Union are organised for European enforcers. For instance, in October 2012, ESMA organised a workshop on new standards (IFRS 10, IFRS 11, IFRS 12 and IFRS 13). Its aim was to describe the main features of these new standards and also to alert European enforcers on some enforcement challenges that the new standards might cause.

IV OVERVIEW OF EUROPEAN ENFORCEMENT ACTIVITIES

59. This section provides a description of the enforcement process undertaken by European enforcers as part of their function of direct supervision of listed issuers.

Description of the enforcement process

60. As previously mentioned, supervisory and enforcement activities are carried out at national level. Nevertheless, matters such as the selection of issuers under review, types of review of financial information and enforcement actions, where necessary, constitute elements which are part of the coordination process at European level.
61. Enforcers select issuers to review based on a combination of a risk approach and either random sampling, or rotation, or both. Risk determination is based on a combination of the probability of infringements and the impact of a potentially significant infringement on the financial markets. Characteristics such as complexity of financial statements, risk profile of the issuer, experience of the management and auditors are also considered.
62. A review of a set of financial statements refers to the process of analysing financial information for compliance with the requirements of the relevant reporting framework. Such a review may cover a company's full set of financial statements and take the form of a full review or be limited to certain areas in a partial review.
63. Partial reviews may be prompted by a number of considerations including: indications of an incorrect application of IFRS and known areas of non-compliance by issuers in previous years, first time application of new standards or areas of particular focus given the economic climate or trading conditions.
64. Enforcers have a range of corrective and other actions, depending on national law, that they may take in respect of infringements of relevant reporting requirements detected as part of the review of the interim or annual financial statements. Where potential infringements of the reporting framework are identified, they are brought to the attention of the issuer. Following exchanges of correspondence and/or meetings with the issuer in which the enforcer may ask for additional information or explanation, the enforcer decides whether the treatment adopted by the issuer complies with the IFRS. After taking into account the materiality of the issue, the enforcer might conclude that the treatment is not acceptable. The case will result in one or more of the following enforcement actions.
65. If the infringement is considered material, the following range of actions are available depending in national law in the enforcer's jurisdiction:
- *Issuance of revised financial statements accompanied by a new audit opinion (where applicable)* - this action entails the withdrawal of the original accounts and issuance of revised financial statements which are subject to a new audit opinion;

- *Public corrective note or other type of communication to the public* - this may mean a press release either by the issuer or the enforcer informing the market of the error and the effect of the corrective action in advance of the issuance of the next annual or interim financial statements; or
- *Correction in the next financial statements* - the issuer adopts an acceptable treatment in the next accounts and corrects the prior year by restating the comparative amounts through applying IAS 8 or otherwise includes additional disclosures not requiring the restatement of comparatives.

66. If the departure from the financial reporting framework is found not to be material, the enforcer sends a notification to the issuer in relation to the departure, but usually this notification is not made public.

67. European enforcers also seek to improve the quality of future financial statements, by engaging in activities designed to provide helpful guidance to issuers in advance of the preparation of their financial information. Example of such activities include:

- *Issuance of alerts indicating the main areas of examination* - many European enforcers announce their main areas of focus for the next reporting period, or preliminary findings of the current examinations, ahead of the next reporting period in order to enable issuers to consider these in preparation of their financial statements.
- *Pre-clearance* - in some jurisdictions, issuers may approach the local enforcer in advance of the finalisation of their accounts and seek a formal decision/advice on whether a proposed accounting treatment is IFRS compliant. The process may differ between countries but it usually takes the form of a comprehensive description of the specific facts and circumstances submitted to the enforcer in writing. The issuer generally provides a detailed analysis of the technical options and/or interpretations, and a rationale supporting his view. The process provides an opportunity to the enforcer to give advice to the issuer in advance of the finalisation of the accounts.

Main indicators of enforcement activity in 2012

68. In order to monitor the level of enforcement activity ESMA collects statistics in relation to the main indicators in relation to the number of reviews performed and the number of actions taken by the European enforcers.

69. In 2012, European enforcers performed full reviews of around 1 050 interim and annual accounts (compared to 850 in 2011) covering around 17 % (12% in 2011) of listed entities accounts in Europe. In addition, 1 200 accounts (1 100 in 2011) were subject to partial review, representing a coverage of 20% (16% in 2011) of the population of listed entities.

70. The coverage of full and partial reviews varies significantly from one country to another because of the diversity in number of issuers per jurisdiction and in the level of complexity of those issuers.

71. Enforcement actions taken by enforcers in 2012 as a result of their reviews were as follows:

- 35 (2011: 18) actions required issuance of revised financial statements;
- around 160 (2011: 150) actions required public corrective notes or other public announcement; and
- around 300 (2011: 420) actions required corrections in future financial statements.

Enforcers also took other actions, such as a notice to the issuer (around 300), but without requiring any corrective action or public announcement.

V ESMA'S CO-OPERATION WITH THIRD PARTIES

72. An important feature in the use of IFRS in Europe as well as worldwide is the need of ensuring that enforcers have a regular dialogue with the standard setter, the IASB, and also with other IFRS regulators.

A) Contribution to the IASB and IFRS IC work

73. As part of its contribution to high quality standards and based on its role of coordination of the European enforcement activities of the biggest financial markets area using IFRS, ESMA has regular dialogue with the IASB and the IFRS IC. ESMA provides the securities regulator's views in relation to enforceability of the proposed standards and ensures that investors' needs are considered by consulting them when needed.

74. A permanent working group, the IFRS Project Group, gathers IFRS experts from 12 enforcers and ESMA staff and meets regularly to discuss developments in IFRS. ESMA has provided comment letters¹⁶ to almost all exposure drafts (EDs) and other pieces of work open for consultation by the IASB and the IFRS IC, including, in 2012, the ED on Investment Entities and the ED on Revenue from contracts with customers.

75. In 2012, EECS met with IFRS IC representatives in order to discuss complex issues identified by European enforcers for which either there is no specific IFRS guidance or where widely diverging interpretations appeared to exist. Among other, the following accounting subjects were discussed:

- Criteria for the extension of the one year period under IFRS 5
- Interaction between the requirements under IFRS 2 and IFRS 3 in the case of a reverse acquisition that does not constitute a business
- Classification of renegotiated loans in the statement of financial position
- Meaning of the "realistic alternative" as part of going concern
- Presentation of items in the cash-flow statement and the comprehensive income statement.

76. The meetings also gave enforcers the opportunity to provide the IFRS IC with feedback on how standards are being applied in practice and to indicate where there might be a degree of uncertainty as to how they are being interpreted. In addition, as part of stakeholder responses outreach requests made by the IFRS IC, ESMA provides an overview on the relevant practices applied by issuers in the EEA.

77. Even if not an official observer to the IFRS IC, ESMA has significantly contributed to the IFRS IC meetings by submitting letters which were included on the IFRS IC Agenda for discussion, such as: the letter on the accounting exposure to Greek Sovereign bonds¹⁷, on

¹⁶<http://www.esma.europa.eu/page/Comment-letters>

¹⁷<http://www.esma.europa.eu/system/files/2012-248.pdf>

the interaction between the scope of IFRS 2 and IFRS 3¹⁸, Information provided elsewhere in the interim financial report and the elimination of intercompany profits between an issuer and its joint venture¹⁹.

78. In 2012, ESMA has taken further steps in its cooperation with the IASB and had two additional meetings in which ESMA provided the IASB Board members with a detailed presentation of the enforcement activities, discussed matters in relation to enforceability of new standards developed by the IASB and areas identified as part of the reviews of accounting practices undertaken by ESMA.
79. ESMA intends to further strengthen its contribution to the IASB standard setting process by engaging actively in future IASB activities in order to ensure that European enforcers and investors views are communicated and considered as part of the overall activities undertaken by the standard setter.

B) Co-operation with other regulators

80. As part of the common objectives of promoting high quality and consistent application of reporting standards and avoiding conflicting regulatory decisions on the application of both IFRS and US GAAP, ESMA and the US SEC considered it important to cooperate and have regular dialogue. Since 2006, the two parties meet regularly to discuss areas of common interest or concern, such as: standards subject to convergence, enforcement related issues, accounting areas of concern in relation to foreign private issuers and other matters related to issuers or market behaviour.
81. As part of the project of considering the use of IFRS for domestic issuers, the US SEC carried out an analysis of how IFRS is applied in practice and published its findings in November 2011²⁰. The conclusion of the report stated that IFRS financial statements generally appear to comply with IFRS. Nevertheless, the report mentioned that transparency and clarity of the financial statements in the sample could be enhanced and that apparent diversity in the application of IFRS may present challenges to the comparability of financial statements.
82. In order to determine the extent to which some of the issues identified in that report required further investigation or particular attention in the future, ESMA launched an analysis covering most of the European issuers included in the SEC's review (representing approximately 80% of the sample). Following that analysis it was found that:
 - a significant number of the issues identified in the SEC report relating to the inconsistent application of IFRS by European listed issuers resulted from different accounting options allowed by IFRSs for which no specific IFRS guidance existed.

¹⁸[http://www.esma.europa.eu/system/files/2012-esma-464 -
esma letter to ifrs interpretations committee on the scope ifrs 2 and ifrs 3 0.pdf](http://www.esma.europa.eu/system/files/2012-esma-464_-_esma_letter_to_ifrs_interpretations_committee_on_the_scope_ifrs_2_and_ifrs_3_0.pdf)

¹⁹<http://www.esma.europa.eu/system/files/2013-9.pdf>

²⁰<http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-paper-111611-practice.pdf>

- Other cases arose because the analysis undertaken by the US SEC was based on a desk-top review and the issues raised were either not material or not applicable.
- In other cases, enforcement actions were already taken by the national enforcer or may need to be considered as part of future enforcement investigations.

83. Nevertheless, some of the topics mentioned in the report were topics previously identified by ESMA as problematic areas and deserving attention as part of the monitoring and enforcement activities. Those areas mainly related to: the use of boiler-plate language in disclosures, presentation of the statement of cash flows and the definition of cash equivalents, disclosures related to financial instruments (in particular relating to judgments used for impairment of financial assets and determining the market for an instrument to be active), judgements related to recognition of deferred tax assets and the determination of post-employment benefits obligations, aggregation criteria used for segment reporting and disclosure of accounting policies developed for accounting for business combinations under common control.
84. With more and more countries adopting IFRS, ESMA initiated contact, in 2012, with other IFRS enforcers with the aim to open future dialogue and exchange practical experience on IFRS enforcement.

Appendix I – List of European enforcers

| Member State | European Enforcer | |
|----------------|---|-------------------------------------|
| Austria | Financial Market Authority ²¹ | FMA |
| Belgium | Financial Services and Markets Authority | FSMA |
| Bulgaria | Financial Supervision Commission | FSC |
| Cyprus | Cyprus Securities and Exchange Commission | CySEC |
| Czech Republic | Czech National Bank | CNB |
| Denmark | Danish Financial Services Authority Danish Business Authority | Danish FSA DBA |
| Estonia | Estonian Financial Supervision Authority | EFSA |
| Finland | Finnish Financial Supervisory Authority | FIN-FSA |
| France | Financial Markets Authority | AMF |
| Germany | German Federal Financial Supervisory Authority Financial Reporting Enforcement Panel | BaFin FREP |
| Greece | Hellenic Capital Market Commission | HCMC |
| Hungary | Hungarian Financial Supervisory Authority | HFSA |
| Ireland | The Central Bank of Ireland Irish Auditing and Accounting Supervisory Authority | CBI IAASA |
| Iceland | Financial Supervisory Authority | FME |
| Italy | Companies and Securities National Commission | Consob |
| Latvia | Financial and Capital Markets Commission | FCMC |
| Lithuania | Bank of Lithuania | LB |
| Luxembourg | Financial Markets Supervisory Commission | CSSF |
| Malta | Malta Financial Services Authority | MFSA |
| Netherlands | Netherlands Authority for the Financial Markets | AFM |
| Norway | Norway Financial Supervisory Authority | NFSA |
| Poland | Polish Financial Supervision Authority | PFSA |
| Portugal | Securities National Commission Bank of Portugal Insurance Portugal Institute | CMVM BP ISP |
| Romania | Romanian Financial Supervisory Authority | CNVMR |
| Slovakia | National Bank of Slovakia | NBS |
| Slovenia | Securities Market Agency | SMA |
| Spain | Spanish Securities Market Commission | CNMV |
| Sweden | Swedish Financial Supervisory Authority The Nordic Growth Market Nasdaq OMX Stockholm | Swedish FSA NGM AB Nasdaq OMX |
| United Kingdom | Financial Services Authority Financial Reporting Review Panel | FSA FRRP |

²¹The FMA will set-up their enforcement activities starting with 1 July 2013 together with the Austrian Review Panel for Financial Reporting that will be established.