



*The Robert P. Maxon
Lecture
2010*



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*The Robert L. Maxon
Lectureship*



The Robert P. Maxon Lectureship

The Robert P. Maxon Endowed Lectureship in the School of Business

The Robert P. Maxon Lectureship was established through Mrs. Dorothy Maxon's generous gift to the School of Business in honor of her husband, Robert Maxon. The GW School of Business oversees the Lectureship and all related events. The endowment underwrites an annual distinguished lecture that adds depth to the business management understanding of the next generation of global business leaders.



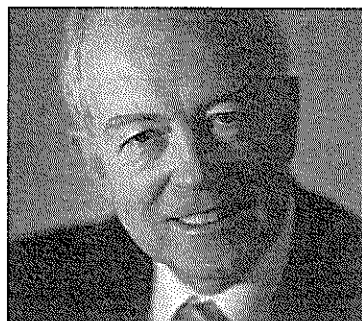
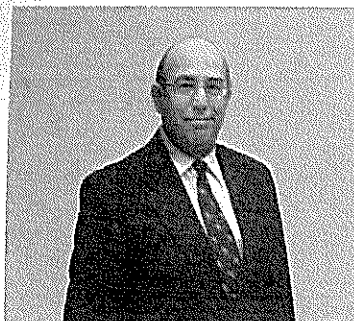


Robert P. Maxon (BA'48)

Mr. Maxon, a highly decorated World War II veteran, earned a degree in business administration from The George Washington University in 1948. He began his career in the energy field shortly after graduating, working in India and later in Japan, at a time when the Japanese were not accustomed to conducting business with foreigners. According to his peers and business associates, Robert Maxon knew how to work with people and build loyalty, and he developed an acute sensitivity to cultural differences. As an executive with Mobil Oil Corporation, he was appointed to a series of increasingly senior posts in Singapore, Thailand, Malaysia, and Indonesia. He later became Vice President of Mobil's U.S. real estate ventures, and retired as the company's General Manager for worldwide corporate public relations in 1983.



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Lecturers*

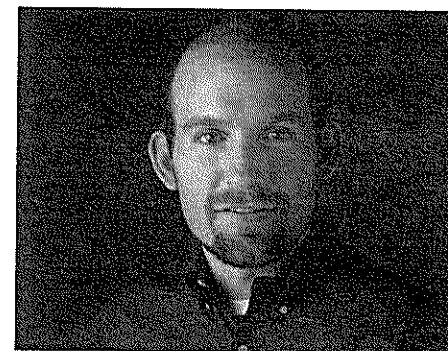


Mr. Robert Herz

Sir David Tweedie

Mr. Herz is in his second term as chairman of the FASB, having served since July 1, 2002. Mr. Herz earned his BA in economics at the University of Manchester in 1974. Mr. Herz is both a certified public accountant and a chartered accountant. Mr. Herz has served on numerous boards and commissions concerned with finance and accounting, including the AICPA SEC Regulations Committee and the Transnational Auditors Committee of the International Federation of Accountants.

Sir Tweedie is chairman of the IASB. Sir David was educated at Edinburgh University (BCom 1966, PhD 1969), where he now serves as visiting Professor of Accounting in the Management School. In 1990 he was appointed the first full-time Chairman of the (then) newly created Accounting Standards Board, the committee charged with the responsibility for producing the UK's accounting standards. He has been awarded honorary degrees by eight British universities, the ICAEW's Founding Societies Centenary Award for 1997 and the CIMA Award 1998 for services to the accounting profession.



Binyamin Appelbaum
New York Times Washington Correspondent

Binyamin Appelbaum is a financial journalist whose work has traced the arc of the economic crisis, from premonitory reporting on foreclosures through recent stories on reforming financial regulation. His honors include the Gerald Loeb Award for Business and Financial Journalism, the George Polk Award for Economic Reporting, and recognition as a finalist for the Pulitzer Prize for Public Service. Appelbaum will join the New York Times this month as a domestic correspondent based in Washington. He was previously national banking reporter at the Washington Post. He is a 2001 graduate of the University of Pennsylvania.

George Washington University
11th Annual Robert P. Maxon Lecture
April 7, 2010

Susan M. Phillips: Good evening. My name is Susan Phillips, and I'm the Dean of the School of Business here at the George Washington University, and I'm very pleased to welcome you to our 11th Annual Robert P. Maxon Lecture. Our program is being recorded tonight. So before I proceed, I'd ask that you take this opportunity, if you've not already done so, to silence your cell phones and any other stray electronic devices you might have with you.

Let me begin by providing a little background on our event for tonight. For those of you who have attended previous lectures, you know that the Maxon Lectureship was established through a gift to the university by Mrs. Dorothy Maxon in honor of her husband, Robert. Mr. Maxon was a highly decorated World War II graduate of George Washington University. He got his degree here in 1948. He began his career in the energy field shortly after graduating, and over the course of his career, he worked in various locales around the world including Japan, Indonesia, and India. Mr. Maxon retired as the general manager for worldwide corporate public relations for the Mobil Oil Company in 1983.

Mrs. Maxon wanted this lecture series to focus on international business in his honor. The topic for tonight's lecture concerns global accounting standards and some might say that this is in fact a foundation for international business. In fact, the question of the relationship between U.S. Generally Accepted Accounting Principles or GAAP and the International Financial Reporting Standards is one of the more interesting and pressing issues facing global investors, business managers, and financial regulators today. In addition, the recent financial crisis and proposals for reforms of financial markets have brought to public light questions about accounting standards and their implications for transparency of firm performance and risk.

So now let's get to the business in hand, and we're fortunate tonight to have with us, not just one, but two eminent figures currently helping to create a clear path for accounting standards into the future.

Robert Herz is in his second term as chairman of the Financial Accounting Standards Board having served in that capacity for eight years. Mr. Herz earned his BA in economics at the University of Manchester in 1974. He is both a certified public accountant and a chartered accountant. He served on numerous finance and accounting boards and committees including the AIC-

PA SEC Regulations Committee and the Transnational Auditors Committee of the International Federation of Accountants. The Financial Accounting Standards Board or FASB is overseen by the Financial Accounting Foundation and is responsible for issuing and maintaining the U.S. Generally Accepted Accounting Principles, or U.S. GAAP. They do so under authority designated by the Securities and Exchange Commission.

Sir David Tweedie is chairman of the International Accounting Standards Board. Sir David got his undergraduate and doctoral degrees at Edinburgh University where he now serves as a visiting professor of accounting in the management school. In 1990, he was appointed the first full-time chairman of the then newly created Accounting Standards Board, the committee charged with the responsibility for producing the U.K.'s accounting standards. He has been awarded honorary degrees by eight British universities, the ICAEW's Founding Societies Centenary Award for 1997 and the CIMA award for 1998 for services to the accounting profession. The International Accounting Standards Board or IASB is based in London and is responsible for oversight of the International Financial Reporting Standards which are used in many countries around the world.

Moderating our discussion tonight, we're fortunate to have with us Bin-yamin Appelbaum. Mr. Appelbaum is a financial journalist whose work includes the recent economic crisis as well as subsequent legislation and proposed financial regulation. His honors include the Gerald Loeb Award for business and financial journalism, the George Polk Award for economic reporting, and recognition as a finalist for the Pulitzer Prize for Public Service. He will join the New York Times later this month as a domestic correspondent based in Washington D.C. He was previously the national banking reporter at the Washington Post. He is a graduate of the University of Pennsylvania.

I want to thank all three of our guests for being with us tonight. I'm sure this will be an interesting discussion. We have reserved some time for Q&A this evening. Note cards are being handed out to you for you to write your questions on, and then our moderator will announce before he gets to the final questions that it's time to submit your questions. And at that time, you can raise your cards and Andrew (he's the one who's giving out the cards now), will then collect your cards. These will then be submitted to our moderator who will put as many of the questions to the speakers as we have time.

So it's time to get on with the program, and as I turn the floor over to our moderator, please join me in welcoming our 2009-2010 Maxon lecturers.

Gentlemen.

Binyamin Appelbaum: So good evening. Welcome to all. To summarize the introduction, on my right we have the organization that sets accounting standards in more than a 100 countries around the world, on my left, an organization that sets accounting standards in the United States and perhaps the place to begin—I know we have varying levels of familiarity with these bodies here tonight—is just with Bob, if you would, tell us a little bit about how that came to be the case.

Robert Herz: Okay. Let me go back about 35 years ago when both of our, actually, organizations were founded (although in David's case, it was really a predecessor organization which then got reformed and we'll talk about that a little bit), but both organizations were founded in the early '70s. The FASB and its parent organization, the Financial Accounting Foundation, were founded really in the light of dissatisfaction with standards being set really in kind of a closed door way, largely by the accounting profession. It was viewed as not transparent, it's not sufficiently independent and the like, and a study occurred and the idea came up that there ought to be an independent group of full-time people who, while their backgrounds might be in accounting and in finance and other realms, ought to independently set the standards and that was the birth of the FASB and the FAF.

At the same time in London, there was a group of globally-minded people; a fellow called Sir Henry Benson who was a partner at Coopers and Lybrand at that time that said, "Gee, with the beginnings of more global commerce, it would make sense to start to try to create some standards that could be used around the world." And so, for the large part of the next 25 years, the two groups worked. There is some liaison, but not that much. The predecessor of David's organization, which was called the International Accounting Standards Committee that was more of a league of nations of part-time representatives, kind of put together to set of standards of what was really best practices from different parts of the world. Some of them were based on U.S. practices, a lot on U.K. practices, and the like, and they also had lots of alternatives, and lot of countries around the world that did not have their own standard-setting mechanisms, smaller economies, would adapt those standards.

In the meantime, U.S. companies have spread kind of across the globe, and their subsidiaries across the globe, and our capital markets continue to attract a lot of foreign companies who wanted to raise significant capital. And so, U.S. GAAP was also spreading around the world because of that.

The increasing globalization (and this is my own take on things), but I think to a certain extent our winning the Cold War, so to speak, and the development of capital markets outside the U.S., in, say, the U.K. and few other places that could actually provide a place for domestic companies to raise significant capital, really gave more impetus to the idea of, well, maybe we ought to get serious about creating a single set of —

Binyamin Appelbaum: Bob, before we go there, just describe, if you would, this unique model that grew up in the United States and why it was important to the capital market.

Robert Herz: Well, the model in the U.S., I mean really came out of the Great Depression I would say, is that along with all the reforms including the establishment of the SEC and the various banking regulators, the idea came that we ought to have a set of uniform accounting principles and disclosure standards and for the public companies, the traded companies, the SEC was given responsibility for both but chose early on to delegate that responsibility to the private sector with oversight. But really, the idea of good disclosure and good accounting being kind of a central element of running sound capital markets and capital allocation was really the impetus for that. A lot of it actually — Susan [Phillips] introduced me, in spite of my New Jersey accent, I actually studied in the U.K. and became a chartered accountant -- a lot of the development of the early accounting standards in the U.S. and actually the accounting firms really traces their origin back to the U.K., to the accounting profession there and the Companies Acts and the like, but we then developed our own kind of model of that which really, I think most people have believed, have been really part of the backbone of our capital markets.

Binyamin Appelbaum: This is a private entity and it's responsible to the SEC and its funding comes from...

Robert Herz: Well, we're a private sector entity. I'd say it's almost somewhere between private and public responsibility. For public companies, we have a delegator responsibility from the SEC, for private companies and not-for-profits, that's through general recognition of our standards including at the non-public level. It's actually state boards of accounting, the licensing organizations that say, "In our territory, in our state, the standards promulgated by the FASB will be the law of the land," so to speak. Our funding comes largely, since the Sarbanes-Oxley Act, from a mandatory fee that is levied on all public companies, both registrants and investment companies, mutual funds, whereby they pay for share of our annual budget

and it's done in the same way as the PCAOB, the Public Company Accounting Oversight Board, which actually oversees the public company auditors. If you're the CFO of U.S. company each, kind of, March, you get an envelope with two bills in it, a large bill for your share at the PCAOB's budget and a much more modest and reasonable bill for your share of our budget.

Binyamin Appelbaum: So that is the FASB. In recent years, you have been leading a push to create a single global set of standards that would incorporate the United States for the first time. That would apply to the United States for the first time. Talk about how that grew up and why that's your goal.

Sir David Tweedie: Well, for a start, can I say, what a pleasure it is to be back here in the colonies to continue the missionary work I have been doing over the last few years...

Binyamin Appelbaum: ...at the George Washington University no less...

Sir David Tweedie: Yes. Finest country anyone ever stole. Basically, Bob was heading in the direction that -- he gave you the background to our predecessor body. Globalization really started about 1975 because previous to that, accounting standards are really created in each country. You got the money from your own country, so it had its own rules.

When I first became an accountant, there were no standards in the United Kingdom. It wasn't total chaos; the firms have kept some semblance of order, but we didn't have any until we had a few crises and that led to the standards coming in. But Bob is absolutely right. In 1973, this group started off and it was a group that ended up with 16 delegations and probably 80 people around the table that met three or four times a year for about four to five days each time, had a staff of five or six, and yet it was supposed to compete with FASB with the seven full-time staff, maybe 40 or 50 at that time. There was just no way it would compete.

The gradual move towards international standards, it started first with the multinationals. They had many subsidiary scattered worldwide. Sumitomo at the moment has 600 subsidiaries using IFRS throughout the world. And you have to translate all these back into J-GAAP or U.S. GAAP, whatever the parent accounting is, complete waste of resource. Well, that was the first start of the pressure, but what really got this going was the Asian financial crisis. You had companies in Asia under their own local standards and they looked fine and then suddenly they went bust. A lot of the money had come from this part of the world and it was just yanked out. It was short term; it was just pulled out; shortage of capital, interest rates rose, investments

stopped, unemployment rose, growth stopped. So we had a major macro-economic issue in these countries; it would probably take them six or seven years to fix their standards. Who is going to trust them having been burned once? So they started looking for a substitute. And there are only two sets of standards really that could be a substitute; the far more advanced U.S. GAAP or the somewhat more primitive International Accounting Standards as they were at that time.

And it was actually FASB and the SEC that said that, really, the world shouldn't take U.S. GAAP in the sense that these were developed for the U.S. markets, it was subject to the U.S. culture, U.S. political pressures, domestic views, and therefore, why should this spread internationally? And it was SEC and FASB who actually set our objective which is one single set of high quality global standards, and that's what we were set up to do. We were set up at the end of the '90s and first met in 2001, and Bob was one of the first board members, one of the founding members. And it wasn't surprising in a way that the FAF trustees asked for Bob to come back to head FASB because they too saw that if we are going to have one set of standards we had to bring the two sets together. So the origins of the IASB lay in this country and that's how it spread.

It's not as easy, having sort of set U.K. standards for ten years. It's quite easy to do that sort of thing, at least in a small country like the U.K. You get the auditors on board; you get the analysts on board; you get the major companies on board, game over. Now you have the French coming out the left field and the Swiss want something different, and cultures are different. In Europe, for example, in the U.K. everything is permitted unless it's prohibited. In Germany, it's the other way around; everything is prohibited unless it's permitted. In Netherlands, everything's prohibited even if it is permitted. And in France, of course, everything is permitted especially if it's prohibited. So you have to deal with this. You're dealing with Japanese, Chinese, and so on, and the U.S. culture. So it's quite difficult to do that.

FASB, we meet a lot now together. Last month, we met on six days, three face-to-face in London; FASB tends to fly because there's five of them and 15 of us, and the other three were on video links to each other. And the idea is we're trying to bring these two sets of standards together, and that's a pretty massive undertaking. And the reason we're doing that is that, in the crisis, there was gradual awareness that we can be picked off. If, for example, a U.S. institution sees something that is weaker in our standards than in U.S. GAAP, they wanted it imported into U.S. GAAP. Similarly, if company sees the same in U.S. GAAP, they want us to do that.

There is an academic theory that it is good to have two sets of standards. They'll compete and the best one will win. Don't believe it. Basically, it's a race to the bottom when you've got that. There's regulatory arbitrage and we've both fought against that and that's really why we believe the best defense is locking ourselves together so there isn't any gap between us and that should be the answer—to have one set of standards—so it doesn't matter if a transaction takes place in Boston or Brisbane or Beijing, we'll do exactly the same thing.

Binyamin Appelbaum: How close are we to that goal today?

Sir David Tweedie: We're pretty close. We started off when Bob took over. It was just after Enron and WorldCom and there was disquiet in the U.S. about accounting, and it wasn't really accounting. This was corporate governance failures and fraud, only a tiny bit of accounting, but the feeling was perhaps, here, we should look outside and see what else is out there. But, in fact, what we did was somewhat rather different. We looked at our sets of standards and said, "Well, if one is clearly better than the other, why doesn't the other one just take it?" And we made an agreement in 2002, it must have been just weeks after Bob came into the chair, that we would look at the reconciliation which existed at that time. If you're using standards from outside the U.S. and listed on the New York Stock Exchange, you had to reconcile to U.S. GAAP. So those using IFRS, it was quite easy because all we did is look at this reconciliation of this income tax, consolidations, and so on. You just run down and say these are the ones we've got to fix. And we started comparing the two and we probably swapped about six each. We took six U.S. standards and FASB and amended six of theirs, but it was taking too long.

And in 2006, the two boards got together with the SEC and said "How do we get rid of this reconciliation? How are we going to bring this closer together so you'll feel happy allowing IFRS to just be used on the New York exchanges?" And the answer was, well, let's set up a program. These are standards that aren't far apart; few principles are different, bring the principles in line. Other standards in both sides are outdated or too complicated. Why don't you, instead of trying to converge and getting converged outdated complicated standard, why don't you actually write new ones together? And that's been the real thrust over the last four years.

Now the G20 tells us they would like that finished in the middle of next year. The SEC road map for making a decision to whether the U.S. moves towards IFRS has used June 2011 as well. And we're under pressure from those countries that are going to change next year, in 2012. They don't want

to change twice, so they want this program finished. And the countries that are changing next year: Korea in March, India in June, Japan who already allow our standards to be used, in August, Canada is going in January; in the following year we've got Indonesia, Malaysia, Singapore, and Mexico. So there's a whole lot that just don't want to have to switch to IFRS and then one year later there's another one and switch again...

Binyamin Appelbaum: And yet despite this momentum, there is still an outstanding question about whether the United States is going to participate in this. Talk about why that is. Why is that not a slam dunk?

Robert Herz: Well, first of all, I think the U.S. needs to participate in it. Some people would have the view that, "Gee, it's kind of like the metric system; we don't need the metric system even though most the rest of the world other than some other places like England don't use the metric system." But I think IFRS, that movement, needs us and we need that.

We are the largest single capital market in the world. We continued to be that. We are the single largest national economy in the world and we have the richest tradition, I think, of standard setting and the notion of what it's supposed to provide, better transparency for investors for the capital allocation objective, and that's not true in all parts of the world. And so, I think if you're going to really have truly a set of international standards and not have the U.S. be part of that, there's a big hole in it, and at the same time, I think that not all aspects of what we do because we're certainly far from perfect, but well, I'll say the good aspects of our DNA, I believe, need to be in that international system.

As I said, it was partly the winning of the Cold War and the fact that other economies started to blossom and create their own capital markets and grow like the U.S. has really given more and more impetus to this whole movement, not only to the standards, the accounting standards, but to other aspects of capital markets integration and regulation and the like. And the U.S. being the biggest economy in the world really needs to be part of that.

Binyamin Appelbaum: You've raised the concern that other countries may not have the same commitment to independence of accounting standards that the United States has demonstrated over time.

Robert Herz: We have something of a tradition which often gets attacked whenever you're in a kind of a rule making or legislative capacity, not everybody is going to agree with everything you propose. And so, in the U.S. as you see, we get attacked from time to time. But every time we get

attacked, for example, last fall there was an effort sponsored by the American Bankers Association to try to really corral what we did through regulatory reform and the response by not only the investment community, but the business community, was swift against that because I think in our country we do have a good appreciation of the importance of having good accounting and good disclosure. And I think that's in part because the wealth of our citizenry is to a large extent related to their investments directly and indirectly in stocks, in bonds, and the like, where that's not true in other countries yet. It's beginning to happen throughout the world as the capital markets develop and as savings buildup in those countries and the like. But we've had the most advanced developed economy and capital market in the world.

Binyamin Appelbaum: You depend for funding on contributions from companies, from countries, and a senior European Union official came out recently and said they were going to hold that funding hostage until you change your structure to include more of the companies that you affect through your decisions, essentially said, you know, we think that this body needs to be more responsive. What's your reaction to that? Are you confident that you have a structure that provides you with the independence you need to set accounting standards?

Sir David Tweedie: I'd better ask my diplomatic advisor if I can answer this question. Am I allowed to answer this by the way I think, Tom? Okay, I won't. Right. What I think of it, it's difficult being either polite or honest. Basically, I think one of the issues that's emerged is that we set the rules at present for 117 countries and it'll be up to 130 by the end of 2012, and you suddenly find in these countries somebody doesn't like these rules. So they go to the government and say, "What can we do about this? Who's doing this?" And they say, "Well it's these nerds in London are making up these wacky ideas." And they say, "Well, what can we do about it?" And the answer is, "Nothing; don't take the standards. If you don't like them, just don't take them." And then comes the pressure, well, we should be able to do something, so what we need is more political control.

And when you look at the FASB, what power has the politicians over FASB? Not a lot, but FASB has its powers through the medium of the SEC. So technically, the SEC could step in. I think it's done it what, twice, Bob, in 30 odd years or something like that. So, what about us? So we discussed the issue of the governance, generally, two or three years back. And the issue for us is we were modeled on the FASB. We had the full-time members; it's full time now of independent people from ten countries, 15 of us and going to 16. We had a set of trustees; five of whom were Americans, 22

trustees in all from all around the world, and they selected the board and they got the finance. What was missing was, well, what's the length of the democratic process after that because these trustees collectively appointed the successors as their terms expired. And the U.S. had it in the SEC and we had nothing.

But when we started, we were, in essence, going to be a think tank. We would just dream up wonderful standards. So if there's someone who wanted a standard on leasing, we could take that one. But after two months of starting, the European Commission decided that all listed companies in the European Union should use our standards, and that made sense because how would you have a single economic market with 27 different ways of accounting with the different member states, so that went through. But we couldn't really get a European SEC; it doesn't exist and that would have been a bad thing because we are not the EASB, we're the IASB, and we didn't want a European focus.

So as, gradually, these accounting standards spread throughout Asia and Canada and so on, and South America, it began to be a way that we could actually see that we could set up, not a global SEC, but we could actually set up a monitoring board which would fulfill the functions of the SEC, making sure the trustees did their job. And the individuals that really formed this were the European Commission, the SEC, and the Financial Services Authority of Japan. They sort of structured it. We have a memorandum of understanding with our trustees, this is how it works. There are five members of this monitoring board: Mary Schapiro, Monsieur Barnier the new EC commissioner, the chairman of the Japanese FSA, the chairman of the Chilean Securities Authority which is the emerging markets representative, and the chairman of the International Organization of Securities regulators technical committee who, happens to be a Dutchman, and he chairs the whole thing. But these are all political appointments. They've all been appointed by their own governments and that links us back in, we're now linked into U.S. through Mary Schapiro and to Europe through the commissioner and to Japan.

The question now is, is that the right body. The Basel Committee is an observer (it's a prudential regulator, not a securities regulator) and it comes to it too. Now, the question is, when you heard that sort of comment coming from Europe saying we're going to look at your funding and that would be conditioned on governance, the question is, well, wait a minute, you set this thing up. This is an agreement between our trustees and this monitoring board. We have to agree to this; at least our trustees have to agree to this. They don't have to agree to it. If you don't want our standards, just

go and do something else. On the other hand, it may be there're some very good ideas to come about what should happen to the monitoring board. If the proposals of the governance mean sweeping away the trustees and putting politicians on to tell us what to do, that would be absolutely unacceptable with the SEC. It would also be unacceptable to the Japanese. They wouldn't accept it. I don't think the Chileans would like politicians telling us what to do either. So it's not as easy as people sometimes think to say, "We're going to force it on you." We are funded at the moment mainly by the levies. Britain has levies. Netherlands has levies. Italy has levies on their recorded companies. Other countries do it in a slightly different way. Japan has agreed to pay so much and it divvies it up among its major companies. Basically, the trustees have set out –

Binyamin Appelbaum: And here, I'm sorry, and here you fundraise basically...

Sir David Tweedie: Well here, this is almost a relic. This is how FASB used to be fund raised. Now, we have no power to levy U.S. companies and that has to be done through the SEC, and the SEC is looking at how it can be done. We have a deficit now, budget, of about two million at the moment. Almost of all of that is from the U.S. in terms of its GDP. It's what we call the "U.S. Gap." It's missing, and you guys are making us take salary cuts—well, not quite—but we're eating into our reserves at the minute, and we've got to try and fix this, but the SEC is working on trying to fix it...

Binyamin Appelbaum: Can this work without a secured, guaranteed funding stream?

Sir David Tweedie: Not necessarily, I don't think it can work. Ultimately, the last thing we want to do is go around and ask companies. That's very 20th century. Now, you want to get levies, and I think the U.S. will find a way of doing it partly short-term and partly long-term. Europe's position is that we, at present, get, I don't know, something like four and a half to five million euros from the European community. Now, the proposal is that the European Commission will supplant that, but giving us less. Now, we don't have to accept that. They could offer it and we could say we don't want it that way. We're not going to take it with conditions, and certainly, I can't see the SEC agreeing to Europe only giving under conditions. Why doesn't the SEC give under conditions and Japan give under conditions? So I just don't think that works.

This is a formula that's been there for two or three years. Funding is conditioned on governance. Well, we met all the requirements for governance,

so what else do they want? So, I think this is still to be explored and there's more to that. But, the fact is, we are a private sector body which upsets some people, but nonetheless, if we don't agree, our trustees don't have to accept. Now, we take the consequences. It may be that some funding falls away and we have to try and replace it, but we don't have to take it, and I think the trustees would not accept money that came with political conditions.

Robert Herz: The accountant in me can't help but make the U.S. Gap a U.S. surplus for you: Our annual budget is, I don't know, something like \$25 million, and we've been spending maybe 70 percent of our time on the international endeavor working with David's folks, so that's about \$17.5 million. Now you have a surplus of over 15 million: in those contributed services.

Binyamin Appelbaum: Congratulations—

Sir David Tweedie: -- And we'll then have to charge for the time for doing your standards for you –

Robert Herz: Europeans might not view it that way, though.

Binyamin Appelbaum: So accounting standards have economic implications; they have regulatory implications; they have huge public consequences. Why should politicians not be involved in the process? What is wrong with a greater degree of public control over something of such tremendous public consequence?

Robert Herz: Well, there are certain elements there to your question. Should politicians be involved? Definitely, they should be interested in it and we welcome that interest in it. As you said, what we do affects companies. It affects the capital markets. It affects the economy. And we do that through the pursuit of what is our public policy objective, which is to create sound accounting, transparent disclosure and the like, and that is our mission. That is our mission under the Securities Acts and under Sarbanes-Oxley Act and it's a sacred mission that we've been entrusted with. And I think the politicians ought to be interested in the extent to which we are effectively fulfilling that mission.

But, of course, sometimes the politicians are interested in us pursuing other missions, sometimes public policy missions or the missions that their particular constituents or special interest groups would like us to pursue. Different industries and different companies are looking to report and portray themselves sometimes in ways that may not... that give them a perceived advantage. They look better than they are. They want an edge, and some-

times they want the edge through accounting.

Bank regulators, who also have a very sacred mission, and there is some overlap between what we do, but it's quite different. The financial stability goal and safety and soundness goal that they have is absolutely sacred and critical to the economy as well, but it's not our public policy mission. And so, the standards we create, while they can choose to use them and they often are very suitable for their use, they also have the ability to create their own capital standards and regulation and the like. To me, it's all about, you know, the word is, "It's all about the economy stupid." We have a very important public policy goal as part of the economic welfare of this country and working with the IASB more globally as well, but that's basically the transparency objective and our public policy mission and that's the one we pursue. Independence can never be absolute. It can't be there without accountability, but the accountability ought to be towards the fulfillment of that public policy objective.

Binyamin Appelbaum: So you raise the banking industry. That's obviously been the flash point in recent times. There's been a lot of pressure on you to adjust accounting standards in ways that it would be beneficial to the banking industry. You spent a hugely unhappy day on Capitol Hill about this time last year, getting yelled at –

Robert Herz: I actually enjoyed it, if you can believe that--

Binyamin Appelbaum: Did you? Oh--it was painful to watch.

Robert Herz: You should have seen some of the hearings on expensing stock options a few years ago. Those got downright personally nasty.

Binyamin Appelbaum: So there's been this sense among the banks, among the regulators, among many members of the Congress, that accounting standards could be a tool to mitigate the extent of this crisis, to help banks get through it. They've really sought your help in doing that and in limited ways you have at times provided it. What have you taken away from that episode? What about –

Robert Herz: Well that episode, I mean that particular episode, I think it's probably not right to correlate events with the causation of events. I mean, we were already in the process of providing some more guidance to deal with what was an unprecedented emergency situation where certain of the fixed income markets just froze up, became inactive. The price discovery was not there. Valuation became very, very difficult in providing more

guidance on how to derive values in that situation. That work was already underway, the folks in Congress, that was in March; I think it was March 12th. The stock market hit its low on March 9th; S&P hit like 666 and people were panicking. There was just palpable fear in the halls of Congress at that point, and what they basically asked us to do, in no uncertain terms, was not telling us what to do, it was just get it done. What you need to do is accelerate what you were doing. I went in there and said, "We'll have it in place for the second quarter," and they said, "That's not quick enough." And so, we responded to that situation but still while maintaining a very robust due process. In fact, over a two-week comment period, we got 700 letters and met with some 50 groups, particularly investors, and I think it ended up with a better product, particularly much more disclosure around these particular investments and the like.

But I view that as an appropriate response in an emergency situation. It's probably -- I wouldn't want to drink from that fountain on a regular basis. But as I said, I think that the politicians naturally have an interest in what we do. It affects their constituents. It does affect the capital markets and the economy, and we're happy to engage with them and explain what we're doing and get their input. What I'm not happy to do is for them to tell me you have to do something that really doesn't serve what is our public policy objective.

Binyamin Appelbaum: You're now considering an expansion of fair value accounting. Banks hate this idea profoundly. Talk about why you think this is important.

Robert Herz: Well, the model we're about to propose (and it is a proposal; I've always found that the reason you go through a due process is because you learn a lot through the input and in the engagement of people), is that we believe that both cost and fair value numbers are relevant and we've seen over history, a lot of history, that particularly loans have been a real problem. The accounting for loans has been a real, real problem particularly in this country, but also in the Lost Decade in Japan, the S&L Crisis, the recent crisis. It was not so much the securities that are traded on the exchanges; the problem were with loans and then loans packaged into securities backed by loans, and the current accounting model, the historic cost accounting model with the management provision for their expected losses has always woefully lagged behind the reality.

Recently, there's been some academic work done that has looked over the last 17 years or so since fair value information has been available for loans and other financial instruments. It looked at the impact of the relationship—

let me put it this way: the relationship between credit risk in banks, U.S. banks across the whole banking sector, and different measures of capital. It looked at regulatory measures of capital like tier 1 capital; It looked at GAAP capital under a current model, then adjusted those numbers for the fair value numbers that are currently in the footnotes. And across the whole banking sector and in terms of individual banks also including banks that failed, it showed that the least correlated with bank credit risk, as measured by credit spreads on their borrowings, was regulatory capital. GAAP capital was a slight improvement over it, but once you adjust it for the fair value of the assets, the predictive ability and the correlation with the credit spreads was like six-fold.

Binyamin Appelbaum: So, this is a more accurate depiction of company's financial health?

Robert Herz: I personally believe it is, but our proposal will show both numbers and it'll actually retain net income the way it is calculated roughly now. What it will do is it will show both the management's view of the situation, the historic cost of the loans, less fair view of credit, on a forward looking basis, but it will also show what a market assessment of the loans is as well.

Binyamin Appelbaum: I'm just pausing to remind the audience that if you have questions, now is the time to write them down and to pass them up so we can collect them.

This will increase the distance between U.S. standards and international standards if this proposal is adopted. It would appear to take us away from convergence rather than towards it. What do you make of the proposal and how much ground still needs to be covered intellectually in order to get to the same place?

Sir David Tweedie: Well, we had a standard that was derived from the U.S. standards to start with, and it probably mashed together about three U.S. standards on financial instruments. And I've often said, if you understood our standard, you hadn't read it properly. It was absolutely incomprehensible, and we had huge fights, especially with the French banks, and we now operate in an atmosphere of mutual trust and understanding with French banks. They don't understand me and I don't trust them. So, basically in this situation, we had a similar thing to Bob because there's been a big issue about un-level playing fields especially when the world is in meltdown. And we got it first of all, I think, in October 2008. We suddenly discovered that the European Commission is going to put through a law to allow Eu-

ropean financial institutions to take securities out of the fair value category into the cost category. Now, under certain situations, rare situations, you could do that in the United States. And we suddenly discovered we have five days to do something and our first reaction was to tell them go jump in the lake, just go ahead and do it. And then after discussion with the securities regulators, internationally and here, the view was if we did that, the European markets could spin out of control because there are no rules whatsoever on how to do it. U.S. has very precise rules. You have to do it in fair value, there are disclosures. There was nothing, because we didn't allow it in the first place. So, the view would be that you get European institutions adding back all their losses, no disclosure, so, nobody would know how these companies were doing, panic would ensue, and the market is going to tailspin. That could affect the U.S. markets.

So we stepped in. We didn't like it. We felt tainted by it. We felt it was a gun to our heads. The alternative of doing nothing was probably worse than doing something, but it wasn't great. So we vowed never again were we going to get into that position. So when Bob appeared in Congress, we could see what was going to happen, and sure enough, it did. My fan club, which is the 27 finance ministers of the European Union, summoned me to come and see them and have a nice friendly chat where they shook me warmly by the throat. So we had this discussion, but we had actually put out a paper saying, "Look, we could do this (the U.S. did), or we could have a full revision of the standard. What do you want us to do?" And we tested this in Asia, Europe, and so on, and the view came, "Change the standards." So when these finance ministers say, "We demand you do exactly the same thing," we said, "That's not the evidence we're getting back."

So we went and we revised it. We simplified the whole standard. We did more outreach on this than probably we've ever done before because we issued a proposal which more or less said that if you can predict the cash flows, and you hold the instrument to collect those predictable cash flows (and we're really talking about interest and principle, so it's only debts and loans--debt, capital, and loans. Anything where it's unpredictable--the exotics, the derivatives, the equities—that has to be at fair value through P&L). So we proposed that. We then went out to over 100 institutions around the world and asked them for their views where we perhaps got this not quite right and so on. So, by the time the exposure period was up, we knew what the reaction was going to be, and we amended the standard and put it out last November. Now it's been adopted in Brazil, Japan, China, Australasia, and they're using it. But the fact that, as Bob said, the income will not be a lot different under the U.S. GAAP than it would be under ours—what we have to try and do is make sure this charge, that goes in the P&L account,

this provision for losses, is as accurate as we can make it. Now we're toughening up our loss provision proposals. Bob's board is going to look at those, we're going to look at his proposals, and the idea's come the autumn, we should try and get a common way of dealing with this.

Now, the next thing is, what are we to do if Bob's FASB go with full fair value and we maintain a split level? We do have a plan B, and the thing is, we must make sure, as best we can, net income is the same. And all we need to do to get that, assuming we have the same provisioning rules, is that we have to make sure that the instruments that we would have at cost—debts and loans—are the ones that FASB would require to be split into credit losses going through income, which we would show too, and the remaining fair value to other comprehensive income which we wouldn't show. But then, we could show the fair value of these instruments, possibly on the face of the balance sheet, so anyone could calculate it in a millisecond. So, okay, it wouldn't be quite the same, but you have to be very bad at arithmetic not to be able to get to the answer within a minute.

Binyamin Appelbaum: There has been this broad trend over time toward providing more and more information to investors, more iterations, which would seem on its face to be a good thing. But there's also this basic problem which Bob had raised a moment ago which is, that if accounting is a language for companies to communicate with their investors the state of their financial health, it doesn't seem to be working very well. We continue to have this problem where companies blink out of existence or suddenly emerge with serious problems and that has not been apparent in their financial statements. We're talking now about a new set of attempts to improve the function of the language. And I guess, you know, in closing before we move to audience questions, I just like both of you briefly to reflect on why that has been such an elusive goal and how confident you are that this latest set of changes will bring us closer to that goal?

Sir David Tweedie: Well, I think, as events happen, you learn from them. You have to be a bit of a cynic in this game. We game our own standards. When you write the standards, you think, well, how are the lads out there going to try and cheat and get 'round it? And we obviously try and avoid the anti-avoidance. But one of the things we are doing (and I think both boards are very strong in this now), is that we're trying to write principle-based standards.

Now principle-based standards are harder to get 'round, because if, for example, I said "If A, B, and C happens, the accounting is X," well, we know the investment bankers will do B, C, and D and say, "Oh, it's different. We

can have Y." But if you have a principle and use A, B, and C as an example, you catch anything generically like that and wrap it up. But you have to watch, with rules they know exactly what to do. And they'll jump out of that sand pit and run naked 'round the beach, and we have to put them back in it. That's part of the game, in a way, to see exactly what happens. So we're improving all the time. For example, you probably don't realize the sheer capital that airlines adopt. One of my big ambitions before I die is to fly in an aircraft that's actually on airline's balance sheet.

Robert Herz: I told him that will be his last flight.

Sir David Tweedie: Well, the thing is, they lease them. And our leasing standards are perfectly harmonized; they're absolutely useless and the reason is that we divide leases. They're both over 25 years old, these standards, not Bob's fault or my fault, but we can have the opportunity to fix them. The leasing industry is about \$700 billion a year; most of it is off balance sheet. But if you see what a lease says, "I promise to pay X per annum for so many years, and I get the right to use this 747 for seven years or whatever," it's not in the balance sheet; I just charge each year what's happening. But I can't get out of that lease. That is a liability, and both boards are adamant that that goes on. Now that's going to change the gearing of companies enormously, and put that on, and on the other side the asset they're using.

Similarly, when we're looking at securitization, you've had the Repo 105 situation. Bob's board tomorrow is looking at proposals that we've developed. We're asking Bob's board to test them to destruction. Any better ideas, we'll look at them. So, we're really trying to make sure—accounting always moves in time, and people will always try and find ways around it. There's always people going to investment banks, "Can you see, there's the rule, can we get past it?" Failing to notice that the objective of financial reporting is a fair presentation, and ultimately, that's what you're after. It's not the rule. It's, are you interpreting in the spirit of what's there? And if you don't—we can write as many principles as we like—if people don't try and show a fair presentation, we're in trouble. They'll run to lawyers and try and get things done.

And one of the problems we have in this country, I don't know if you've heard, but Harvard Medical School are now using lawyers instead of mice in experiments and that's because in the United States you've got more lawyers than mice; and lawyers will do things that mice refuse to do; and you get fond of mice. But we've got to stop this sort of legal mentality. We're actually there to try and ensure what happened, and what we do,

both boards, is try and show these standards so the accounts do reflect the actual economics and that's what we're both straining to do. And, okay, sometimes, we might not get it quite right, but I think when you look back at what accounting was ten or 15 years ago and where it is now, it's vastly different and vastly improved, and we're getting more sophisticated. Having leases on banks is going to make a huge difference.

Pensions, you know, the pension scheme deficits were smoothed out of the way. If you had a pension scheme of assets of 40 million and liabilities of 40 million and the assets fell 10 million, you have a deficit of 10 million. But that's not the way we showed them. We sort of said, "Well, you know, it's a long-term thing, and some of that fall will be market noise. You measure that at ten percent, whatever's the higher--assets or liabilities." Well, liabilities at 40, so you take four million off the ten million and you're down to six million. And, of course, it's a long-term thing. Spread that over the working lives of the employees, say ten years; you end up showing a deficit of 600,000.

Now you explain that to your grandmother. You may as well take the 10 million, divide it by the cube root of the number of miles and the moon, and multiply it by your shoe size. It doesn't mean a thing, and yet that was how accounting was. Now FASB changed that a year or so ago. We are changing it this year. In the U.K., they did it that way for the last ten years, but that's how accounting is developing. Actually, companies are only now discussing the major deficits they've got because we didn't account for them properly.

Binyamin Appelbaum: Let me put the same question to Bob if I can. Obviously, we're dealing with many of the problems that emerged during this last crisis. Are we getting ahead of the curve? Is principle-based accounting a way of getting ahead of the curve as David has described it?

Robert Herz: Well let me go back to your basic question and I agree with a lot of what David said. I mean, I think there are a number of factors. One, as David pointed to, people just disrespect, violate the rules, cheat. I mean, that's not something that as standard setters we can directly deal with. That's up to other people, enforcers and then legal. You can set rules or laws but people do violate them and that continues to happen. They do it where they perceive a risk-reward in doing that. That will always be the case. It will always continue.

The second thing is that, as David said, accounting has lagged economics, accounting standards. I feel very strongly to that effect. And every time we

try to move accounting towards economics, there's a huge fight. There was a fight over stock options, accounting those as part of compensation. There was a huge fight back in the '80s when the FASB first said you're going to have to account for your pension liabilities and for your healthcare, post retirement healthcare liabilities. You can't just do it on a pay-as-you-go basis. These are real liabilities and the companies that were most affected, the auto companies, the smokestack companies, said these were not real liabilities. Well, 20 years later, we know they were real liabilities. We know there are real liabilities at the States. We know that the government's social liabilities are real liabilities.

I think we're going through some of the same aspects right now with the idea of how to measure certain financial assets. We're going through some of the aspects that David said would, showing leases on balance sheet as commitments and the like, and so, there has been, to my way of thinking, a slow catching up of accounting to the underlying economics.

You have to remember that the financial statements consist of several statements. There is cash flow statement which showed the actual cash flows for the period. There is an income statement which shows what was earned during the period, but there's also a balance sheet. The balance sheet has been the weakest sister of all those three statements historically. It has been kind of just the residual of what the income statement has been, and there has been reluctance to kind of measure things at current value rather than historic cost and allocations of historic cost and things like that.

The third factor, getting to the financial crisis, no accounting can deal properly with a situation where no one knows what the values of particular assets are. You take a CDO or CDO squared, and when the trading stopped and you look at those instruments, thousands of loans underlying the basic CDO and then pieces of those rearranged in a very complex structure with derivatives embedded in it, and there's no standardized information underlying that.

In order to do any valuation, whether you call it current value or you do what you think your credit losses are going to be, you have to be able to project future cash flows or ranges of cash flows. The fact that there was no infrastructure supporting those markets, that was the biggest crime along with others, the poor underwriting and the rating and all that. But accounting struggles in that kind of situation because you don't know how to account for those things other than cash as it comes in and that's very unsatisfactory.

Binyamin Appelbaum: So turning to audience questions because this one is

relevant. Even before the crisis, there obviously were issues with the way that accounting was conducted by these companies. So, our first question from the audience, "Do you have plans to look into the accounting issues raised in the Lehman report as the SEC is doing?" I know you just touched on the ways that you're addressing this; perhaps go into a little bit more depth about that.

Robert Herz: Well, the SEC is in the middle of large inquiry process, what they call the "Dear CFO" letters. They've sent letters to all the major financial institutions over the past few weeks trying to understand whether Lehman was a one-off or it was broader. If it was a one-off, then maybe we have something where, in that situation, a company that was in trouble chose to make itself look a little better than maybe it was and that ought to be dealt with through those processes. If in fact people were more broadly interpreting the accounting rules and even the disclosure requirements in the same way, then there's stuff for us to do.

Binyamin Appelbaum: Do you agree?

Sir David Tweedie: Absolutely.

Binyamin Appelbaum: All right, "The joint projects FASB and IASB are addressing are on a fast track. Why?"

Sir David Tweedie: Well, we've been looking at these projects since about 2006, and I think the crisis made governments aware that accounting really mattered. And you started finding governments... we even discovered, for example, that President Barroso of the European Union, Angela Merkel, President Sarkozy, and Prime Minister Berlusconi actually spent half an hour discussing our financial instruments standard. Now I'd have loved to listen into it. It's amazing heads of states are actually involved in these things, and we get heads of state writing to complain about us, but I think what it did do, it alerted people to the issue that accounting really had to depict what Bob was just talking about, the economics. And sometimes the answers can be very, very uncomfortable and that's where we almost go right back to where we started in the beginning. Sometimes people don't want to see the uncomfortable numbers.

In the crisis, there were great temptations for politicians to say, "If you can just hide this, with a bit of luck, it will all come good." And we had that before in the sovereign debt crisis, that was hidden, because accounting was very primitive in those days, but you had some banks that quite frankly were bust. If we'd have been brutal, we didn't exist at that time and neither did

Bob—well, Bob existed, but not in his present role—but the sort of thing there was that you had banks full of these sovereign debts. Nobody expected countries would default, but they did. And had we said, "Write them down, bang, now," then we would have a situation where a lot of our major banks were bust. So the regulatory authorities said, "Well, why don't we just allow you to write them off with this formula over a period of years," and that's what happened, and their argument then, "Phew, well that saved our banks!"

The question is, and Bob will almost certainly support this, what if we started showing what the market had thought of those banks? Would they have kept lending—these loans, rather? If you lent to the South American country and it was at 100 and now the market showed it was 95, would you keep lending when it had it gone down to 80, knowing that the market was expecting a 20 percent loss? So there are signals and they weren't missed, and I think part of the issue now is how do we get to a situation where we can reflect that?

It's going to be uncomfortable, and can people accept it? As Bob said, the trouble with accounting, getting it back to the economics, is people often don't want it at the economics, and that's where we have to try and get the herd moving gently in the westerly direction without stampeding the thing. We're in change management. That's our job. And that is quite hard because we're salesmen, ultimately. We're not just producers. We've got to sell this thing, and we've got to persuade people this is the right answer, take this; it's tough, it's hard, but it's good for you. "But my bonus is tied to this year's profit, not next year's; I don't want this number," and that's when the pressures come in and that's where had the issues on share-based payments and all these issues.

Binyamin Appelbaum: You're gracious enough not to name any of those banks. Citigroup, of course, is the preeminent example and it has been raised as a question, "What would have happened if market discipline has been imposed on that company in the late 1980s? What would they have been doing over the last 20 years differently than they were?" But underscoring the importance of accounting standards brings us to this next question.

Bob, "Why should the U.S. give up control of something so important as accounting standards?" And because you've talked a little bit about why you think that is a good idea, could you also address how you think you might be able to overcome what is probably very widespread hesitations about this idea.

Robert M. Herz: Yes. I think it's a good idea, but I also think we need to do it right. The long-term cost/benefit to us, I think, can be significant, but the short- and medium-term cost/benefit is harder to see because we already have a pretty good system. From the companies' points of view, their view is a lot of change, cost in the system and the like. People are used to that now. Our convergence efforts can mitigate those costs because the closer we come together, the less the switching cost and the like, but it's got to be done right. That's why I said that I think it's important that we be part of this system with our heritage and our experience and our tradition of trying to have as independent as possible capital markets standards information for investors.

It's important because we are going to continue to be a major part of the world economy in dealing in trade and capital flows and M&A with all sorts of other parts of the world. Therefore, it means a lot to all our citizens, our investors, that we have a good global capital market system and that we have that supported by good reporting and good accounting. So, in a global situation, you're never going to have control. That won't work. That in part seems to be what Europe tries to do with David in the party.

So you have to create a structure that is consonant with the market that it serves. If we're going to have global capital markets, you have to have global capital structures. We need to be a very important part of that, an important seat at the table, and make sure that our interests are served without dictating to other people and that's a fine balance in any kind of international endeavor, but it's the way the world is going.

Binyamin Appelbaum: Does the U.S. risk losing "market share," as it were, if everyone else adopts a system that is as trusted and as successful?

Robert Herz: That's always the -- the protectionist kind of view of life. I've lived in various parts of the world and I do believe in getting to global solutions where we can as long as they're balanced and they're crafted with everybody's input. They may not fit perfectly -- they are not going to serve each individual country or group exactly like they like, but I do believe that they will create a rising tide all over, economically, and that will be to our long-term benefit. Sure, there are going to be short-term losers, there's no doubt. We see that in industries as things shift and the like, but it's very hard to turn back those tides.

Binyamin Appelbaum: You basically have a year to convince Mary Schapiro that this is a good idea. How do you do that?

Sir David Tweedie: I don't think we need to convince Mary it's a good idea. I think she believes it's a good idea. I think what we have to try and do is do exactly what Bob said. We're in a situation where we have a plan. It's now part of the SEC road map. People want us to finish this and they want us to finish it within 15 months. That's a tough call. The boards, the efforts that have gone into it, the fact that Bob's team is flying across every second month, virtually, to London, and we spend the best part of the week discussing it has made a huge difference. Previously, we discussed it, some other time Bob would discuss it, and then we'd think, "Gee, we don't get the same answers." Then we have to have some phone calls and things between us. Doing it all together has speeded the whole process up. And we have to try and make sure the answers we get are of quality that is a big improvement on what we've got and high-quality standards.

And the fact is, the rest of the world—its almost the antithesis of the question you just asked Bob—the IASB firmly believes that the U.S. has a central role of playing in all this in the future. But it is hard when you're a sovereign country that says, "Well, I control this at the moment. Why should I give this up?" And that was the same in Britain, that was the same in Australia, the same in Japan. People don't like it. And it's putting it into the common good, and they do that because there are advantages in it.

The U.S. world capitalization is falling. If you look at the share in the world capitalization of the U.S. eight years ago, it was 52 percent of the stock exchange capitalizations worldwide. Now it's 35; at least it was in 2008; it's probably less now. It's Asia that's growing. But the U.S., as Bob said, has the tradition, the Anglo-American tradition—which is part of the reason we fight with Europe, because they don't have that—is very, very strong in accounting and we need the U.S. in there. And North America has guaranteed, out of the 16 board members, is guaranteed at least four; Europe four, Asia-Oceania four, Latin America one, Africa one, and two floating. You will have a major core in that once you've made the decision to come in. And I think frankly U.S. will make the decision in due course, next year some time. You will have time to get ready for it because it will be 2015 unless you're a multinational and there's an option given and you go early.

The other aspect of it is the rest of the world is tired of the convergence program. We think it's absolutely essential that we bring U.S. GAAP and take the best of U.S. GAAP into the international community, but if you are someone in some other country outside saying, "Well, why is this favored nation status? Why not us as well get involved with it?" And the answer is because there are two main sets of international standards, one U.S. GAAP

and one international GAAP. Other standards don't even come anywhere near that, and the obvious thing is to bring the two together. But there is resentment. "If the U.S. doesn't want to do it, get them out." We hear that all the time and we're ignoring it. "Change the work program. Drop some of the subjects. Do this instead because I want this done. Why should we wait?" Well, the reason we should wait is the prize is enormous. This is probably one-in-a-generation chance of doing what the SEC and the FASB set out for us ten years ago: one single set of global standards. Often I liken it to the fact when I was at school, I used to play in goal for the school football team. And in the cup semifinal, we're winning one-nothing in the last few minutes, and this forward broke through and he hit the ball so hard it went past me before I could move. Fortunately, it hit a post and rebounded to him. He hit it first time and this time I threw myself to the left and turned the ball around the post, and my teammates we're absolutely ecstatic. What they didn't realize is I was trying to save his first one.

Binyamin Appelbaum: Here in the colonies we call it soccer.

Sir David Tweedie: Yes, soccer. We don't; we gave that up. But we won't get another chance at this. If this fails, it won't just be U.S. GAAP and IFRS. I can see it fracturing. You get, why should Japan come in, why should Latin America? The have to make their minds up; the whole thing could blow apart and that's a big problem.

Robert Herz: That's part of the tension here is that other countries in the world want to come in and as David said do not want to change twice, yet we have to get this right. I would hate to think that for the sake of six months or a year, we would get it wrong, because the standards we're going to create could be in place for many, many years. We have to make sure we've given it our best shot and that's why we've intensified our processes, and we're going to intensify our engagement processes.

But I do have some concerns about -- certainly in the U.S. prospective, we are tossing out there something like eight, nine, ten proposals all at once on revamping just the most major sections of accounting practice and all of that. The ability to get the standard right, as I said, really depends on getting good input.

Binyamin Appelbaum: There is a sort of elephant in the room. We've not mentioned its name at all tonight, but it's China: an emerging economy, growing capital markets, increasing role in all of this. How do they fit in?

Sir David Tweedie: Well, in 2007, China dropped its communist-style

standards, and they adopted, but not quite adopted, IFRS in the sense that they took the principles out of IFRS, put them in the law, and then took the remainder and made it mandatory guidance from the ministry of finance. Now, the deal is you get the same answer and through Hong Kong, we checked it and they do virtually. There is one or two small bits, not major, but the answer is -- and we say it to China, "You need to go word for word."

Robert Herz: They have a little bit of a Chinese menu approach in that they take the IFRS standards, tailor them to the Chinese situation. They've taken a few of our standards and tailored them to the Chinese situation. They seemed right now to kind of like that approach of kind of being -- I call it, "Almost hurts."

Binyamin Appelbaum: So we now have three international standards?

Robert Herz: Well, it's pretty close too. I mean the thing you also have to recognize is that a lot of the international standards that David inherited in his book of standards were actually crafted from U.S. standards.

Sir David Tweedie: The Chinese quoted companies, Bob is right, they took the best of the American standards, but we took them too. So the quoted Chinese companies are pretty well in the IFRS. Not some of the others, but the quoted ones are pretty well there. We're telling them too, they are looking at, sort of, keeping up to date all the time. It is much easier if you adopt, because otherwise there may just be a question mark that you're not quite there. And moving onto the changes that they're going to have to make as this program moves through—one of the things that I've always said, giving advice, I'm almost reluctant to give advice. I remember when I moved to my present home in Edinburgh, they have had a rather unusual plant in the front garden which looked like overgrown parsley, but the neighbors who didn't like the lifestyle of the previous occupants thought it was marijuana, and I was bit concerned about that. So I called in a horticulturist and he gave me advice I never forgot. He didn't know what it was either, but he said, "Look, if you're worried about this plant," he said, "Pick it, dry it, and smoke it, and if you're still worried about it, then it's parsley." But the advice we give countries is, take the standards. We have in our constitution a rule, that two years after implementation, if we discover problems, we'll come back and look at it.

By that time, the cohort of board members who were there originally would have changed slightly. There'll be new ideas in there, experience of what's happened. We can change it again. So our view about 2011 thing is we can make massive differences: the leasing standards hugely different; pensions

on balance sheet; consolidations; control not 50 percent plus one of equity. These are major changes. Now, maybe at the edges we can improve them further and we can still keep doing that and that's really what this is about. It's moving the game forward, dealing with the things that we were talking about with people who are coming in, and playing games, best we can, stop them. But it also needs good auditing and it needs good regulation. So we're only one leg of a three-legged stool, but we're going to keep the game going forward and that's actually a role in the meantime.

Binyamin Appelbaum: Thank you very much.

Susan M. Phillips: Ladies and gentleman, this has been a wonderful discussion, and I think as you can well imagine, we could probably go on all night, but I'm going to intervene at this time and thank Sir David Tweedie and Bob Herz for coming and sharing with us their perceptions and insights on the current discussion of international accounting standards. Please join me in thanking them.

We have a plaque for each of you to commemorate your participation in the Robert P. Maxon Lecture, and there's also a permanent plaque that resides in the business school and your names will be added to that. So thank you both very much for joining us, and ladies and gentleman, please come back next year for the 12th Robert P. Maxon Lecture. Thank you very much and good evening.



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