

Department of Business Administration

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Enforcement of IFRS in Sweden

-Achievements for building trust for the financial information



Abstract

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Key Words

Enforcement, IFRS, OMX, FI, CESR, Trust

Purpose

Has the trust changed for the Swedish financial reports based on IFRS standards with the enforcement work done by FI and OMX, and if so, why?

Methodology

The study was conducted through an abductive approach and a qualitative research strategy using a hermeneutic epistemological stance. The data was collected using interviews and respondents selected with a purposive sample technique.

Theoretical perspectives

We have used perspectives related to the concept of trust in business and enforcement of IFRS in order to grasp their relations. Trust is fundamental when working with surveillance and financial statements.

Empirical foundation

With interviews as a data collection technique, we have gathered data from five respondents representing larger listed companies, auditors from the four largest auditing firms, and from the enforcement bodies FI and OMX

Conclusions

This thesis has found evidence suggesting that trust towards the financial statements has changed, unfortunately to the worse. Although there is a perception today among preparers (the companies) and attesters (the auditors) that the work contributes to a creation of trust, the magnitude and actual impact are hard to specify. Due to the transparency, competence and impact of the surveillance made by the former enforcement body Övervakningspanelen, there is not an increased trust towards the financial statements in comparison to the situation today.

Abridgements

CESR	The Committee of European Securities Regulator
FI	Finansinspektionen
IAS	International Accounting Standards
IASB	International Accounting Standard Board
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard
LVPM	Lag om värdepappersmarknaden
NGM	Nordic Growth Market
OMX	Nasdaq OMX Stockholm AB
SEC	Securities and Exchange Commission

Clarifications

Attesters	The auditors
Börsen	OMX
Enforcement bodies	FI and OMX
Prepares	The companies
Respondents	The auditors, the companies, FI and OMX
Surveillance	The word surveillance is used synonymously with enforcement

**□ Instead of going to war, we are now using EU as a
democracy platform to solve issues □**

Göran Persson, Prime Minister in Sweden 1996-2006

Preface and Appreciation

It is not a cliché. Our interactions with other countries have increased tremendously. A milestone has been the way we are communicating with each other. Another is the way of transporting ourselves and other goods. Another is the way of using democracy as a tool for development.

We can go on forever and name major breakthroughs in mankind, but that is not our intention in this thesis. Our goal is to write about one very important puzzle in the big EU machinery, or for that matter, called a major breakthrough. But instead of just naming it, we will explain, discuss and analyze it and make it a useful source of document.

It is not a false statement to say that the EU system has self created our topic as a necessary component for the economic development. Look upon it as a cause and effect theorem where the cause is a more globalised environment and the effect are rules for making that happen. Or take the example of the Egyptian pharaoh's, where the cause was a belief in a life after death and the effect was the creation of modern architecture when they build the pyramids.

Spring 2009 has been a very intensive, hectic, stressful, demanding, difficult, melancholic and just as wonderful a spring in Lund can ever be. We are confident that this period in life will be the most valuable time we ever had in school. Challenges only makes you stronger and more prepared to face future challenges, and that is a part of what life is all about, is it not? Who knows what challenges we will be facing spring 2010, but at least we can say that we are prepared, down to our bones.

We want to thank our friends and family for supporting us during this thesis and our mentor Kristina Artsberg for her valuable input. We also want to thank all our respondents for participating in our interviews, thanks a lot!

Lund, May 30th 2009

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1.

Background

This chapter aims towards introducing enforcement and trust, as these are the major topics in this thesis and declare the problematic aspects of the same. This chapter shall also show why enforcement and trust are interesting to study and the issues related to the work with it today in Europe and Sweden. The discussion will result in specification of a problem and a purpose.

1.1 One Single Market as the Spark to Convergence

It started back in 1951 when France, Germany, Belgium, Luxembourg and the Netherlands signed a treaty to tie their coal and steel industries together. Six years later, they signed the Treaty of Rome, creating the European Economic Community, better known as the European Union. The goal for the union is to create one single market for goods, one single market for services and one single market for capital. One single market for all of Europe that helps to bring down barriers, create more jobs and increase overall prosperity. Despite its achievement so far, the work is not done yet. Creating a single market is not a finite job; look at it as an ongoing task that needs constant effort and improvement (European Commission, 2009).

The idea has created strife not only for taking down tolls, but also creating similar rules and standards to be applied over Europe. One of them is the creation of one single accounting standard. Researchers like Wong (2004:25) state that the convergence to a single set of accounting standards is for the best interest of the public and contributes to efficient capital flows within and across country borders. The former Senior Associate Chief Accountant from SEC, Ms. Susan Koski-Grafer (2005:8) puts it like this:

"I personally am looking with optimism to a day when investors around the world can look at the financial statements and disclosures of listed public companies everywhere, reports that have been prepared -- and audited -- using improved, more comparable standards than today, regardless of where the company is based and in what markets the company's securities are listed."

One breakthrough was when the EU released its Regulation 1606/2002 which stated that listed companies in each member state shall use International Accounting Standards (IAS) endorsed by the European Commission from 2005 and onwards. But it was not only countries in the EU that adopted the International standards. Countries like Australia (Aasb, 2009) and China (Acca, 2009) have followed and are using standards prepared by IASB. It even seems like the USA intends to change from their US GAAP to IASB (Accountingweb, 2008).

Over the course of time, different countries like the ones mentioned above have developed their own system of accounting. Today there are major international differences in accounting practices that are affecting the convergence process due to, among other things, cultural

differences. The most important direct cause of the financial reporting differences is separated into systems with:

1. Credit-based financing system and with relatively unimportant outside shareholders, and;
2. Those with important equity markets and many outside shareholders.

The countries that have important equity markets and many outside shareholders leads to a system with decision-useful accounting, to a separation between tax rules versus accounting rules and a large auditing profession (Nobes & Parker, 2006:37-8).

Another obstacle in the convergence process apart from cultural differences is the dilemma observed by Street, Gray & Bryan (1999:46). They investigated 49 major companies' 1996 financial reports from 12 different countries claiming to use IFRS. The result showed that only 41 % of the companies noted compliance with IFRS despite claiming to do so.

"Achieving true convergence of accounting standards - convergence of not just the words, but also on a shared understanding of the principles and objectives - is a costly and time-consuming objective. It is, however, the right objective and one that must be pursued vigorously, as it offers tremendous opportunities for all involved, but especially for users and preparers of financial statements." (Tokar, 2005:710)

1.2 The Vital Role of Enforcement

The EU Regulation 1606/2002 number sixteen also states that:

"A proper and rigorous enforcement regime is key to underpinning investors' confidence in financial markets. Member States /---/ are required to take appropriate measures to ensure compliance with international accounting standards".

Dao (2005:108) argues that it is not likely to achieve a qualitative financial reporting environment by just making it regulatory for companies in EU to use IFRS. This also requires a procedure to oversee the application of the standards. Researchers like Hope (2003:238) as well as Leuz, Nanda and Wysockil (2003:523) agree and argue that the quality of financial information depends on both the quality of the accounting standard itself and how effective the enforcement bodies are doing their job. The World Bank's Report on the Observance of Standard and Codes (2004:3) even argue that setting accounting standards are important, but enforcement of these standards are even more important. The lack of a mechanism to ensure compliance with established standards contributes to a weaker financial reporting environment.

What does then a proper and rigorous enforcement regime really mean? The organization for the accounting profession in Europe, The Fédération des Experts Compatibles Européen (FEE) representing over 500,000 accountants, defines the enforcement activities as:

"All procedures in a country in order to assure the proper application of accounting principles and standards. Efficient enforcement should be made up of due process and economic efficiency, the essential performance measure being to deter harmful violations. A key feature of enforcement is to be able to require the restatement of financial statements that do not comply with applicable accounting standards." (FEE, 2001:8).

FEE also made in 2002 what they consider to be features for efficient enforcement and what enforcement bodies should consider when building such an organization (FEE, 2002:8).

FEE's Features for Effective Enforcement bodies:

1. Support for high quality corporate governance and external audit
2. High quality, expert, globally-consistent decisions on important issues
3. Freedom from bias
4. Transparency and clear procedures
5. Confidentiality and speed of action
6. Avoidance of making detailed accounting rules
7. Focusing resources
8. Rectification of defective financial information
9. Sanctions

These features will be described in more detail in chapter 3.6 *Essential Features for an Effective Enforcement Body*.

1.3 The Responsible Bodies in the Enforcement Process

The Committee of European Securities Regulator (CESR) is responsible for coordinating the enforcement of IFRS in Europe. The organization was created in 2001 as a response to the upcoming plans of introducing IAS as a mandatory requirement for listed companies. Therefore, each member state in the EU is responsible for organizing the enforcement mechanism. This approach differs from the one used in the USA where SEC is the overall responsible body for enforcement and each state doesn't have their own organization for enforcing the US GAAP accounting standard (CESR, 2009).

The responsibility for enforcement in Sweden is regulated in the law "Lag (2007:528) om värdepappersmarknaden" (LVPM) that was mandatory as of July 1st 2007. The law says that the body which has the final responsibility for enforcement in Sweden is Finansinspektionen (FI). FI has delegated the actual enforcement procedures to two largest stock market places in Sweden: Nasdaq OMX Stockholm AB (OMX) and Nordic Growth Market (NGM). OMX and NGM have to report to FI about their activities and all other information that FI finds necessary to secure a sound financial market. The FI organization has more power and more sanction capability than OMX and NGM have, but it doesn't mean that FI should revise their decision. The only time that will happen is when the OMX and NGM possibilities are not enough (Hjelström, 2007).

1.4 The Strife and Difficulties with Enforcement

Sanctions when violating the IFRS standards according to CESR should make sure that correct information is delivered to the market. Each member state in the EU is responsible for sanctioning companies in their countries. The punishments are in other words not harmonized and there are different solutions amongst EU countries (Norberg & Thorell, 2009:117). Brown and Tarca (2005:204) also expect different solutions for enforcement between countries when the topics are reflecting national issues, including each country's existing institutional framework for financial reporting. The reason for these different approaches is a matter of interest for future research.

In another article, Brown and Tarca (2007:459) continue to discuss IFRS as a principle based standard. In an ideal IFRS world, the users' would make consistent decisions about application of

the system. The standard however, is perceived as principle based and users must make decisions on how to interpret the standards. The interpretations involve individual judgment and that will lead to different decisions from directors, auditors and enforcers both individually and in other countries, they continue.

The discussions about principle versus rules are important for the future development of accounting standards and how to enforce them. According to Benston (2006:171), there has been an increase in pages of IFRS with added guidance to the standards. Zeff (2007:293) also mentions the growing length in IFRS standards from 1200 pages in 2000 to 2300 pages in 2006. The discussion about principle versus rules has raised the question as whether IFRS are moving towards a more rule based standard rather than principle based as reflected by the increasing length and greater details.

Another issue, by examining the accounting policies disclosed in the financial statements, is how the enforcement bodies can determine if the company complies with the measurements and practices described in the accounting standards. This is difficult, or even impossible for an enforcement body to determine, because of the need for professional judgment when interpreting the standards. The user needs to therefore rely on auditors as the principal line for detecting noncompliance with standards (Dao 2005:125).

Norberg & Thorell (2009:125) say that there has not been any argument about having an enforcement mechanism and there has also not been any further discussion about when to take action. They ask the question: "what function does the enforcement play and how should it be done to best fill its purpose?" Their benchmark is that auditing is the primal tool to strengthen the financial information towards the shareholders. That leads them to the question why auditing needs to be complemented with enforcement. Enforcement and auditing seems to be two parallel but separate functions with an unclear inter relation.

Nobes and Parker (2006:175) on the other hand are claiming that the audit is a necessary component of the monitoring and enforcement process, but it is unlikely to be sufficient. Auditors are perceived to have difficulties being independent, so they can benefit from an enforcement body since the enforcement bodies only means is to qualify the auditors' opinions. Enforcement bodies cannot also check the financial information in detail and have to rely on external auditors in this case. The existence of enforcement bodies will strengthen the auditor to insist in compliance with reporting standards.

1.5 Specification of Problem

As the purpose of enforcement is to prevent and identify errors in the financial statements, as mentioned earlier in this chapter, we find the concept of trust to be an interesting aspect in this thesis. Dao (2005:108) argued that to achieve a qualitative financial reporting environment there is a need for procedures to oversee the application of the standards. Leuz, Nanda and Wysockil (2003:523) agreed, and said that the quality of the financial statements depends on the effectiveness of the enforcement bodies. However, we find that one can always question if the enforcement is efficient enough to increase the trust towards financial statements. Can an enhanced regulation increase the trust towards annual reports and, in turn, prevent future financial scandals? Does the work of CCSR and FI/OMX increase the trust towards the financial statements?

Due to the past ethical financial scandals, e.g. Enron, concerns have been raised towards the accounting and auditing professions (Copeland, 2005:35). Furthermore, trust is a foundation for

markets today, and its relevance and importance in the economy is evident (SOU, appendix, 2004:12). Today, there is a focus of trying to sustain trust between actors through regulation. Trust needs to be maintained on a regular basis, and this is a common feature of regulatory relationships. A successful regulation and a legitimate compliance must be represented by a mutual trust between the regulatee (the companies and the auditors) and the regulator (the enforcement bodies FI and OMX). This involves actions that are appropriate and necessary by the regulator, as well as, from the regulatee's perspective, there should not be abuse of trust by actively not following agreed standards (Clarke, 1999:25,146).

Studies show that the existence of regulatory institutions is not enough to control actions. There also has to be trust between people, and more importantly, between larger actors acting in the economy. This trust involves the notion of confidence that others follow laws and regulations, and that it is possible to rely on people to follow written and oral agreements. Not only literally, but also relying on people to understand its true underlying meaning. It is the dominance of such attitudes in a society that contribute to the creation of economic growth (SOU 2004:75). An efficient cooperation is created through the work towards common means, which only can arise through trust (Rothstein, 2003:21-2). How is it in Sweden today? Do users and creators of the financial statements trust the work of the regulators? Is it so that investors, and other users interested in the financial statements find there has been an increase in the trust towards the annual reports in Sweden?

It is well known that auditors have a fundamental responsibility to ensure the credibility and trust for the financial information, but what about the credibility that the Swedish enforcement agency brings? It is important to grasp knowledge and perception about the enforcement bodies (FI and OMX) to actually determine the trust for their work and towards the financial statement. This leads us to the research question:

1. How is FI and OMX's work perceived today by attesters (the auditors) and preparers (the companies)? Is there room for improvement or a need for it in general and if so, why?

The concept of trust has a fundamental meaning and it is important that a successful regulation and a legitimate compliance must be represented by a mutual trust between all parts involved. Trust in this thesis can be discussed at two levels; trust between the enforcers of financial reports (the enforcement bodies FI and OMX) vis-à-vis the preparers of financial reports (the companies) and trust between enforcers of financial information (the enforcement bodies FI and OMX) and attesters (the auditors) of financial information. This leads us to the research question:

2. Is there a trust from the preparers and attesters for the work with enforcement of IFRS today done by FI and OMX and if so, how is it expressed?

Consequently, the purpose of this thesis is; has the trust changed for the Swedish financial reports based on IFRS standards with the enforcement work done by FI and OMX, and if so, why?

1.6 Purpose

When having the above background discussion and specification of problems in mind we can again state our purpose:

- Has the trust changed for the Swedish financial reports based on IFRS standards with the enforcement work done by FI and OMX, and if so, why?

We aim to elucidate the trust aspect among creators of financial statements when considering the work of enforcement today done by FI and OMX. As this has not been investigated before, what we are aware of, we will explain the situation today and the effect it has on the financial statements. Further, this research aims to suggest improvements on how the surveillance system in Sweden can better function if there is a need of change.

1.7 Delimitations

During the formation of the purpose, and the specification of problems, we have made delimitations. As stated above, this thesis will investigate how and why the trust for financial statements has changed. Although investors are the main users of the financial statements, they will not be investigated. The intuitive way of studying the enforcement and trust aspect related to CESR would have been to actually grasp their opinions. Despite this, we find it interesting to, as a first study within this field what we are aware of, study the opinions and views of the creators of the financial statements. Through this, this thesis includes the creators.

The creators are represented by attesters (the auditors) and preparers (the companies), as well as the enforcement bodies (FI and OMX) responsible for the surveillance today. NGM are not included as one of the enforcement bodies, only FI and OMX represent their views mainly due to time and financial restraints. Another issue with this subject is the problem of finding anyone who possesses adequate knowledge. As this is a new subject, due to issue of LVPM in 2007, we considered the creators of the financial statements to actually be the ones, despite the enforcement bodies (FI and OMX), with most knowledge and input to this thesis. Without their aspects, it would not be possible to reach a trustworthy conclusion related to why, if, and how the trust has changed.

Further, we also saw an opportunity to take advantage of our own interests and study it from the perspectives that we find most fruitful and interesting. As we have a major in auditing and accounting, the inclusion of attesters (the auditors) and preparers (the companies) adds an additional interesting aspect for us specifically, which is another reason for their enclosure. As Saunders et. al. (2007:23) suggests, one is more likely to do well while investigating a topic and field of specific interest. To fully grasp and understand if the financial information has been affected by the enforcement directives from CESR and if it really fulfils a function, it is important to contact and discuss the subject with the actors working most closely to it. Therefore, from this aspect, investors in this case we find would be the next step to include if investigating the subject further.

These delimitations will result in an exclusion of the views from the main users. Although this will affect the empirical findings, the opinions and views gathered from the creators of the financial statements and the enforcement bodies will add an interesting aspect to the work with enforcement today and the aspect of trust in relation to the financial statements. Further, through this choice of scope in the thesis, we find the possibility of giving suggestions on improvements larger as there will be an insight in the reasoning and opinions of the enforcement bodies (FI and OMX) as well.

1.8 Disposition

1. Background

- The chapter aimed to introduce enforcement and trust, as those are the major topics in this thesis and declare the problematic aspects of the same. The chapter has also shown why enforcement and trust is interesting to study and the issues related to the work with it today in Europe and Sweden. The discussion resulted in specification of a problem and a purpose.

2. Method

- This chapter provides a presentation of how to investigate trust towards financial statements. Moreover, sample and the choice of interviews as a data collection technique will be discussed, as well as, the reliability and validity of our conclusions. The first part of this chapter is an introducing section describing the scope and data collection more briefly.

3. Frame of Reference

- It is essential to have a solid theory to support your argumentation in the conclusion. In this chapter, we are presenting organizations which are responsible for the enforcement process in Europe and Sweden. The concept of enforcement is closely linked to the topic of trust and we will show why it is necessary to discuss these two concepts as parallel phenomenon. We will end this chapter by presenting how different organizations define the enforcement process.

4. Empirical Findings

- In this chapter we aim to present the answers from our interviews. The respondents consist of five large listed companies, the big four audit companies plus FI and OMX. The first part of this chapter corresponds, to the major part, to research question one, and the second part to research question two, as far as it is possible. Thus, we find the answers to somewhat overlap the two research questions.

5. Discussion About the Empirical Findings

- Chapter five, *Discussion About the Empirical Findings*, will guide you through a discussion where we interpret our empirical findings with help from the frame of reference. With guidance from the research questions and the purpose we aim to suggest in the following chapter how the enforcement bodies (FI and OMX) can build better trust towards the financial statements. As mentioned in our method, the benchmark for what is good enforcement is what preparers (the companies), the attestors (the auditors) and what FEE consider it to be.

6. Conclusion

- Trust, as we have learned through this thesis is a fundamental and crucial aspect for parts involved when creating financial information. We want to conclude our discussion from the last chapter in this conclusion and, as stated in the purpose, make suggestions on how FI and OMX can build a better enforcement system with trust as the foundation.

7. References

2.

Method

This chapter provides a presentation of how to investigate trust towards financial statements. Moreover, sample and the choice of interviews as a data collection technique will be discussed, as well as, the reliability and validity of our conclusions. The first part of this chapter is an introducing section describing the scope and data collection more briefly.

2.1 Overview of Data Collection and Scope

To answer the purpose in this thesis we have decided to use a qualitative research strategy, further, we justify our findings and choices using a hermeneutic epistemological stance. With interviews as a data collection technique, we have gathered data from five respondents representing larger listed companies, auditors from the four largest auditing firms, and from the enforcement bodies FI and OMX. The respondents were selected using a purposive sample technique based upon the level of information possible to obtain.

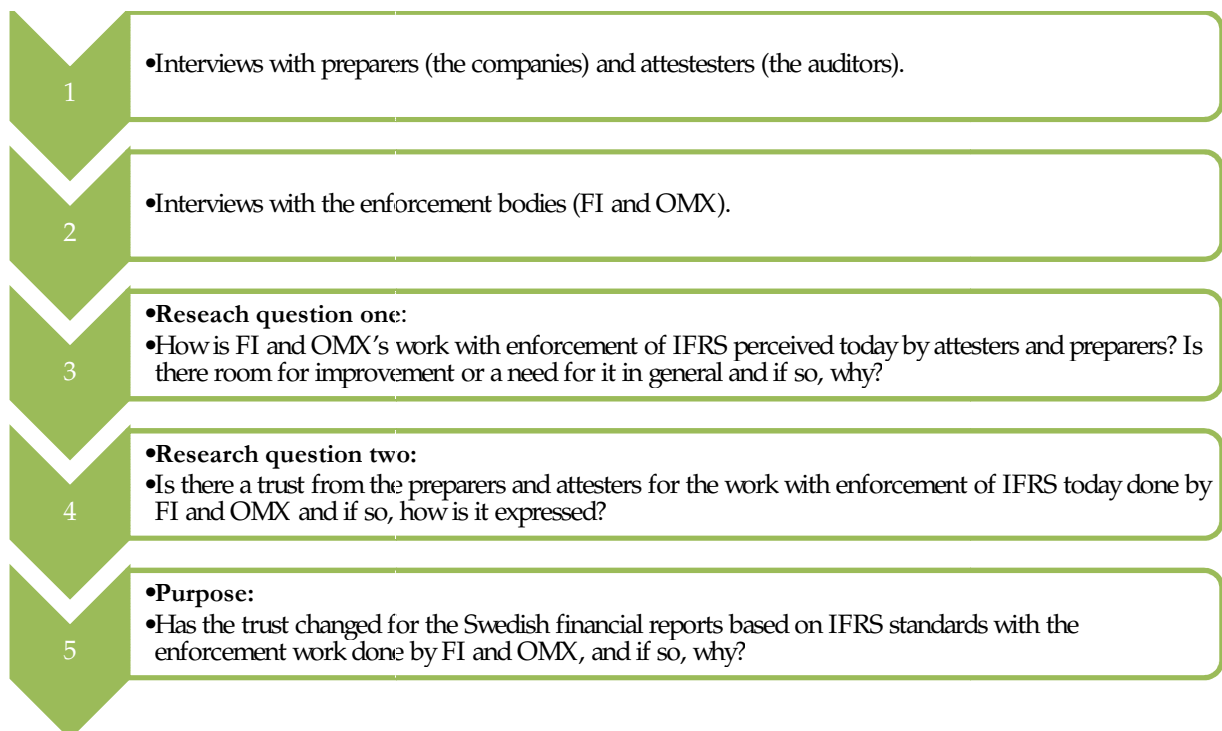


Figure 1 Overview of Data Collection and Scope

As illustrated above in Figure 3 *Overview of Data Collection and Scope* the first part involved the interviews towards preparers (the companies) and the attesters (the auditors). These questions were similar and, all but one interview conducted via telephone. The second part of the process concerns the interviews with the enforcement bodies (FI and OMX), also conducted via telephone. These questions were somewhat reconstructed to also incorporate some of the aspects brought forward in the first step of the data collection process, but also due to that not all were relevant to ask.

The empirical findings were later coded and discussed using the structure of the research questions, and the last part of the thesis answer the purpose in relation to the empirical findings. The interview questions were based upon and influenced by both chapter 3 *Frame of Reference* and the empirical findings, as mentioned above. This to be able to make assumptions about the overall perception of how enforcement of IFRS is proceeding in Sweden and in turn relate this to the aspect of trust.

The preparers (the companies) are represented by five larger firms all listed in Sweden, the attesters (the auditors) involves the four largest auditing firms and the enforcement bodies (FI and OMX) are represented by one person each. This sample is illustrated as a triangulation, in Figure 4 *Triangular Approach*.

2.2 Research Approach

Studies conducted are either inductive or deductive. A deductive approach starts with theory where commonly hypotheses are defined, which in turn affect the whole study. An inductive approach, on the other hand, starts with empirical observations and analysis, which yield hypothesis and possible new theories (Befring, 1994:14). This thesis, however, has an abductive approach due to the use of existing theory, while, at the same time, considering the views and opinions of the sample under investigation to reach analysis and conclusion.

The abductive approach can be explained as a combination of induction and deduction and is said to generally have a stronger inductive approach. Abduction is a way of combining practice and theory, which is illustrated in Figure 1 *Abductive Approach*. It aims to describe the subjective and social practice as thoroughly as possible, while at the same time enabling critical analysis of the data (Wigblad 1997:32-4).

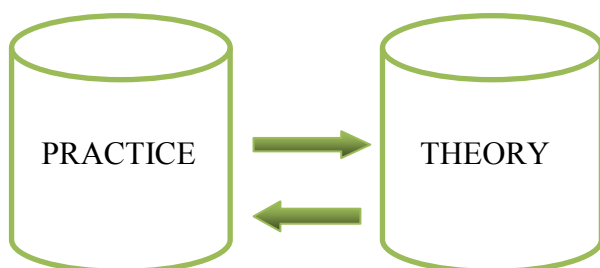


Figure 2 Abductive Approach (Wigblad, 1997:27).

In contrast to Wigblad's (1997:32-4) statement that generally abductive approaches are more towards the inductive, we have an approach more towards deductive. This since we make use of research questions based on theory, and complement with empirical observations to reach answers and conclusion. However, as this subject has rarely been investigated before in Sweden,

what we are aware of, we believe that the study will also have an inductive character. This is due to the possibility of reaching new conclusions about this subject.

Another aspect to consider when deciding upon a research approach is what purpose the research should have. For instance; whether it should be descriptive, exploratory or explanatory. However, a research project may have more than one purpose. To begin with, a descriptive study may act as a forerunner to further explanatory or exploratory research (Saunders, Lewis & Thornhill, 2007:132-133). Since the approach taken in this thesis has not been studied before, and can therefore shed new light on the trust aspect of increased regulation regarding the financial statements in Sweden, the objective is partly descriptive. A descriptive study can be seen as a forerunner to an exploratory research, where the objective is to seek new insights and to assess a phenomenon (Saunders, et. al., 2007:133). Through this, the thesis will also take an exploratory objective as why there has, or has not, been a change of trust towards the financial statements will be studied as well.

2.3 Qualitative

When conducting a study, there are generally two different strategies to choose between; qualitative and quantitative. A qualitative study is characterized by a more insightful data collection with deeper understanding, in comparison to a quantitative approach (Befring, 1994:15; Taylor 1998:4). It can also be described as a study that generates non-numerical data (Saunders et. al., 2007:134). Whereas, a quantitative study, on the other hand, refers to a type of collection, which enables a map out, and explanation of a subject in form of variables and quantifiable relationships (Befring, 1994:14).

The advocates for quantitative methods criticize the supporters of qualitative methods and say that quantifiable investigation is always to prefer, due to the level of accuracy. There is an inability to quantify social relationships, as there are not sufficient instruments for measurement (Andersen, 1994:112). As the findings from qualitative studies change over time and new actors replace old, studies of this character are rarely static (Loftland, 2006:72). There are also difficulties involved when considering the possibility to counter reply a qualitative study, due to its unstructured character and dependency on one's own level of resourcefulness (Bryman & Bell, 2005:64).

Despite this, we consider the benefits to outweigh the costs of qualitative methods and find this method to be the most appropriate when considering the purpose with this thesis and what we are aiming towards finding. As we intend to gain a deeper understanding and gather insightful data, the most suitable choice of method is qualitative. Although, a quantitative study enables the researchers to collect data that can be generalised (Saunders et. al., 2007:134), we find the relevance of the data, in our case due to lack of time and resources, would be jeopardized as the insightfulness and relevance of the results would decline. Only the larger limited companies listed in Sweden, specific experts in the larger auditing firms and the enforcers are likely to have sufficient insight to this subject of interest. Thus, there is a clear qualitative approach in this thesis.

2.4 Epistemological Stance

There are two larger platforms within epistemology that affect and justify the choices of method and benchmark. These are positivism and hermeneutics (Lundahl & Skärvad, 1992:38). The later

is connected to potential justifications of undertaking a qualitative investigation (Denzin & Lincoln, 2003:294).

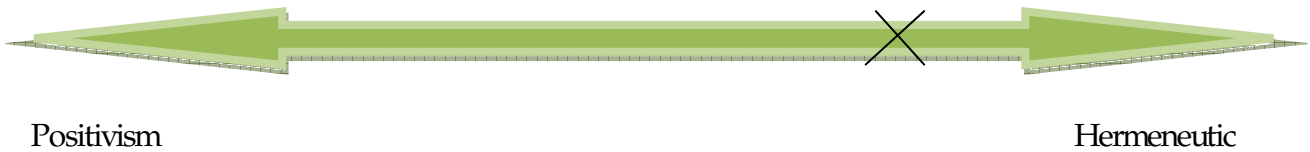


Figure 3 Epistemological Stance

As illustrated in Figure 2 *Epistemological Stance* above, we have a hermeneutic epistemological stance in this thesis, due to our qualitative research strategy. This perspective is a way of trying to understand human actions, various ethical commitments, and different perspectives of understanding and analysing the validity and objectivity. Hermeneutics states that understanding is about interpretation (Denzin & Lincoln, 2003:294; Alvesson & Deetz, 2000:157; Lundahl & Skärvad, 1992:42). This understanding is an essential part of the interpretation and will show the character of a phenomenon e.g a text, an action or a statement (Alvesson & Deetz, 2000:157). The investigation should aim towards understanding how other people experience their situation, and how this, in turn, may affect decisions and actions (Lundahl & Skärvad, 1992:43).

The hermeneutic stance in this thesis is characterized by interviews where we will try to create an understanding of if, how, and why the trust has changed for the financial reports in relation to the directive from FI. Through this, we leave the positivistic stance completely as we do not separate facts and views, as Lundahl and Skärvad (1992:39) states as one of the most fundamental stances when considering positivism.

2.5 Process of Gathering Data

To answer the purpose of this thesis, both secondary data and primary data have been collected. According to Saunders et. al. (2007:606, 611) secondary data can be defined as data originally collected for some other purpose. Furthermore, primary data is described as the data collected for this specific thesis. In the next two sections we will describe the collection of the two types of data.

2.5.1 Secondary Data Collection

To be able to build a frame of reference, as can be found in the next chapter, and gather information to the background there was a need for secondary data. To a larger extent we have used scientific articles, which can be found in databases via the University Library, such as ABI/Inform and Google Scholar. These databases have been browsed using words and combinations of "enforcement and trust", "trust in business", "trust and accounting", "enforcement and accounting". Further, we have also used books from the library, SOU and home pages.

When using secondary data it is important to critically examine the content as it may not always originate from impartial sources. Some sources could even be considered incomplete and biased. (Lundahl & Skärvad, 1999:223). Data from larger organizations is often considered to be more

truthful (Saunders et. al. 2007:265). The secondary data used in this thesis have been collected carefully. The mix of scientific articles, books and information from larger organization's homepages contribute to a trustworthy secondary data.

2.5.2 Primary Data Collection

Depending on the choice of research strategy and research approach, there are different types of data collection techniques to choose from when collecting primary data. We have decided upon interviews as the basis for the data collection in this thesis, as mentioned earlier in this chapter. In order to grasp the opinions and views of the creators of the financial statements under investigation, we found interviews to be the most accurate. A questionnaire may have revealed if the trust has changed, but not illustrate the 'why aspect' as thoroughly as interviews. Through interviews we were able to get more freely spoken answers, and through this to make more fruitful interpretations and understandings. As Saunders et. al. (2007:312) and Lundahl & Skärvad (1992:115) also states, interviews may give the researchers valid and reliable data that is more relevant for the research questions in the thesis.

One can separate interviews between structured, semi-structured, and unstructured. Unstructured interviews are most common when considering qualitative investigations, and are characterized by:

- An aim towards trying to get the interviewee to share opinions and values, while at the same time talking about hard facts
- Information based questions are complemented by questions aimed towards trying to get the interviewee to elaborate on his/hers own thoughts and opinions. (Lundahl & Skärvad, 1992:117)

We find our aims and interests are best in line with unstructured interviews, this is also the way we chose to go about when collecting the relevant information. The interview questions were constructed both from chapter 3 *Frame of Reference* and from our interest, in other words, from purpose and research questions. These can be found in Appendix 1-3.

The process of interviewing can be divided into two parts. To begin with, we interviewed attesters and preparers and asked them the same questions. This since the interview questions are to some extent also directed towards the trust and competence of the enforcement bodies. See illustration in Figure 4 *Triangular Approach*. The second part of the interview process concerns FI and OMX. The interview questions used in these interviews differ to some extent from the one used towards preparers and attesters. These since some of them were no longer relevant from their point of view and others were interesting to ask as they have a different perspective than the attesters and preparers.

Choice of data collection technique should not primarily be decided upon money and time (Wigblad, 1997:82). Despite this, these two factors have been decisive when deciding upon techniques for data collection in this thesis. The interviews are conducted via telephone, mainly due to limited time and financial resources. However, one of the attesters chose to answer the questions via e-mail. The ten telephone interviews were made in Swedish and all answers were translated before inclusion in the thesis. During the questioning notes were taken, and some of the interviews were recorded, and immediately after completion we wrote out fairly while the discussions and reasoning made by the respondent still were recallable.

2.5.3 Critique Towards Using Interviews as a Primary Data Collection Technique

Due to our background, perceptions and interpretations we affect how we understand the answers the interviewee will give us. Many times we omit from ourselves when we judge another person and the reasons to his or hers actions. Through this, we may find situations during the interviews where the interviewee is perceived to have completed an answer; however, it is not as exhaustive as possible. This answer may later be completed by the interviewer self (Ekholm & Fransson, 2002:82). Andersen (1998:99) calls attention to the risk associated to interviewing people in leading positions. These persons are used to decide and talk gladly about what interests them specifically, which may not always be the same as the interviewer is interested in. Ekholm and Fransson (2002:74) point out the risk of restraining the respondent when recording an interview. This since some may feel uncomfortable by knowing that their answers are recorded and there is a risk of someone else listening to it later on. Instead one should consider taking mental notes during the interview. This will also lessen the time spent on compiling the findings.

We have taken these limitations into consideration and find that the benefits outweigh the disadvantages of using interviews. However, we recorded the first interview but found that the risk of restraining the respondents were too high and decided instead to take mental notes during the interview. Through this we also had more time to compile and discuss the empirical findings than would have had if we used the recorder consistently. As all of the respondents have leading positions the knowledge of them to maybe be interested in talking about aspects more in line with their interests during the interviews, were noticed by us. However, as we were aware of this likelihood we were also prepared to ask them the same question again and tell them to try to stay in line. However, we find that due to that the interview questions not were very controversial; a direct contact with the respondents would probably not resulted in more thorough answers than what we got by using telephone interviews.

2.6 How Did We Select Our Respondents?

There is a triangular approach to the sample in this thesis, see below in Figure 4 *Triangular Approach*. The sample consist of attesters, preparers and enforcement bodies; all different creators of financial statements and interested and affected by the financial information in different ways.

The sample consist of representatives from five larger listed companies in Sweden representing the preparers, four employees from each of the four largest auditing firms representing the attesters, one from OMX and two from FI corresponding to the enforcement bodies.

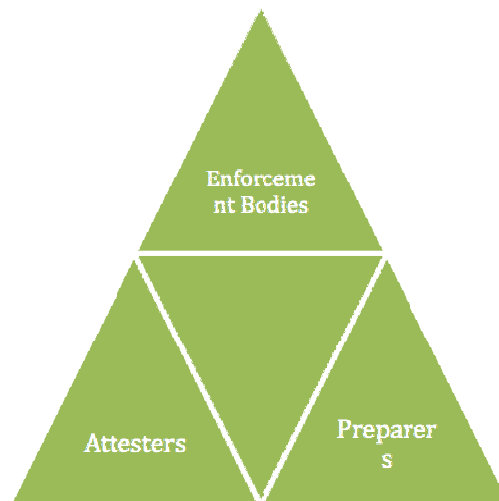


Figure 4 Triangular Approach

Saunders et. al. (2007:207-8) mention different sampling techniques, and divide them into two groups; probability sampling and non-probability sampling. As we have not used a probability sampling technique, due to the help from Claes Norberg, we can label this approach as non-probability. Saunders et. al. (2007:230) discuss a sampling technique called 'purposive sampling', this is also what we find is most similar to the process we have used. Purposive sampling enables the researchers to include respondents that are particularly informative.

As this subject calls for expertise, it was of high importance to reach the correct people working closely with this topic. Through this, Claes Norberg, former professor at the University of Lund, suggested some names of people he knew had the knowledge and expertise. Through this help, we were able to contact and include the most appropriate people for our thesis. If we were to find these people on our own, we would have spent more time finding the respondents, and through this, maybe in the end we would not have had time to include as many as we actually did. One can also speculate whether we would have been able to include the same people at all. We appreciate Claes Norberg's help, as from previous investigations we know this could become a time-consuming process.

2.7 Analysing Data

2.7.1 Coding

Coding is a process of defining and sorting the collected data- it is about putting like-minded pieces together and through this, create an organized framework. In turn, the researcher is able to place the various data into meaningful sequences (Glesne, 1999:136). This is how we have summarized the empirical findings. For example when considering the interview question about a definition of trust this question was summarized into the three words; clearness, consequence, and mutual understanding, however, the question was also complemented with an interesting quotation.

Through this method the data collected and presented in chapter 4 *Frame of Reference* is more concise. Further, the empirical findings is divided according to the structure of our research questions and in relation to the interview questions, this to create a structure that is easy to follow for the reader. Although we have coded the answers to some extent, we have still made use of quotations, as can be found in chapter 3 *Empirical Findings*.

The process of putting the pieces in agreement together was made through a compilation of the answers under each and every interview question to start with. Through this we were able to create consequential summaries of the responses. The deviant answers we found relevant to include can also be found in the empirical findings, most of them are integrated as quotations. Furthermore, due to the number of open-end questions and, through this, a large differentiation in answers, we have used quotations.

2.8 General Critique of Method

After completed this thesis we find it would have been interesting to follow-up the empirical findings with complementing interviews. This to make use of the triangular sample consisting of attesters, preparers and enforcement bodies. If this would have been the case, we would have been able to use the differing and contrary statements and challenged the respondents using the others answers. Through this process the respondents would have been able to elaborate further on specifically interesting statements and in some cases also been given the possibility to defend themselves. Secondly, we find that OMX are subjective to this topic, as they already have publicly declared a disinterested towards conducting the surveillance any longer. Through this their statements become biased.

These two limitations would have been easily solved. After a process of coding and compilation complementing interviews via telephone could be accomplished easily. A limit of only a couple of questions would have given the thesis more interesting empirical findings to rely upon. Further, by including NGM instead of OMX we could have decreased the risk of subjective answers as NGM, what we are aware of, has not publicly announced an unwillingness to conduct the enforcement of IFRS. If we were to do the same investigation one more time, these two limitations would have been corrected.

2.9 Reliability

The definition of reliability is:

“the extent to which data collection technique or techniques will yield consistent findings, similar observations would be made or conclusions reached by other researchers or there is transparency in how sense was made from the raw data.”
(Saunders et. al., 2007:609).

In other words, the result should not be affected by the researcher undertaking the investigation. Reliability is crucial for the creation of validity and is often done by some kind of standardisation to ensure the investigation is undertaken in a consistent way (Lundahl & Skärvad, 1992:152).

There are threats to reliability:

1. First, subject error may affect the findings; however, it is relatively easy to control. Subject error is avoided by not interviewing on Monday afternoons and Friday afternoons, which may impose different results due to the moods of the respondents.
2. Secondly, findings may be subject to interviewer and interviewee bias. The first is where verbal tone and comments can affect the response to questions. It may also be the case that the interviewer creates bias in the way the answers are interpreted. Interviewee bias, on the other hand, relates to the possibility of the interviewee's perceptions about the interviewer.

3. Thirdly, there may be observer error. This type of threat to reliability involves risk of bringing forward answers. This is avoided by using a high degree of structure in the interview.
4. Fourth, and last, is the issue of observer bias, which involves the risk of interpreting the results differently (Saunders et. al. 2007:149).

As mentioned earlier, this thesis is created through both primary data and secondary data. When considering the secondary data we find it to have high reliability. This due to that the articles and books used are screened and processed before being published. We also find the homepages used to sustain a high reliability due to the issuers.

The primary data may be a threat to the reliability as it is gathered through telephone interviews. However, the risk of subject error is low as the telephone interviews are conducted on different days and at different times. From this perspective, the threat of reliability is minimized as the respondent's answers not all are affected by a particular mood during a certain day.

One should not underestimate the possibility of interviewer bias and interviewee bias. We are aware of its likelihood, which is also why we have conducted the interviews two and two, as far as it has been possible. All but two interviews have been conducted by both of us at the same time, this to be able to sustain as low subjectivity as possible. We asked every second question to minimize the risk of changing the verbal tone and additional comments in relation to reactions on the previous questions and the answers. Through this, we find that we have a low risk of bias in our empirical findings. However, it is almost impossible to fully protect the findings from any bias when conducting an interview, in comparison to the likelihood of interviewer bias through a questionnaire. Despite this, we are positive that if any other researcher or researchers had conducted the interviews, the findings would have been similar.

Observer error may impose a threat to reliability on our findings as we have used the opportunity to ask resulting questions. However, this type of questioning is used among all interviews and almost always with the same questions. Through this, we find it not to threaten the reliability significantly. When considering subject bias among all the respondents we find the likelihood of subject bias to be low. This since they are all working in a managing positions and is influential managers themselves.

2.10 Validity

Validity concerns the extent to which the data collection method and the research findings measure and are really about what they aim towards being. Further, the concept of validity can be subdivided into internal and external. Internal validity refers to the importance of correct data collection technique and how it should measure and convey what it was intended towards doing. External validity, on the other hand, refers to the generalisability of the research results (Lundahl & Skärvad, 1992:150; Zikmund, 2000:281). The issue of external validity will be discussed separately under the section 2.9 *Generalisability*.

The inclusion of the enforcement bodies in this thesis may also affect the validity of the findings. This since there is a possibility that they have answered the questions with a somewhat restriction knowing that what they say may harm them in the end. Therefore, we would like to emphasize this possibility as the findings may be somewhat affected by this. Furthermore, it may also be the case that other events happening outside our knowledge have affected the interpretation of

whether the trust towards the financial statements have changed, and if so why. The respondents may have answered the questions with this in mind, although we are not aware of it.

We find that the secondary data used, as well as the primary data collected through interviews, help us to answer the purpose with this thesis. Through this, validity in this thesis is achieved. The use of the empirical findings in combination with the frame of reference contributes to the research questions' answers, as well as the answer to our purpose.

2.11 Generalisability

Generalisability, also called external validity, involves the notion of whether the findings in this thesis can be applicable to other research settings. Non-probability sample cannot be considered as statistically representative for the whole population (Saunders et. al. 2007:151).

Despite that findings through a non-probability sample cannot be generalised statistically to an entire population, we still find the results to some extent be generalisable. As it is mainly the preparers whom could be represented by others and through a larger sample, the findings can be considered somewhat generalisable and can be applied to other research settings. However, one must bear in mind that it is not feasible to make too broad generalisations by only studying it from smaller samples, as we have done. However, we find the results in our study to engender logical generalisations anyway.

2.12 Chapter Summary

To answer the purpose in this thesis we have decided to use a qualitative research strategy, further, we justify our findings and choices using a hermeneutic epistemological stance. With interviews as a data collection technique, we have gathered data from five respondents representing larger listed companies, auditors from the four largest auditing firms, and from the enforcement bodies FI and OMX. The respondents were selected using a purposive sample technique involving a selection based upon the level of information possible to obtain.

In the next coming chapter the frame of reference will be presented. This includes a more thorough explanation of enforcement in Sweden today and the enforcement bodies responsible. In addition, the concept of trust and its relation to business is clarified.

3.

Frame of Reference

It is essential to have a solid theory to support your argumentation in the conclusion. In the following chapter we are presenting the organizations responsible for the enforcement process in Europe and Sweden. The concept of enforcement is closely linked to the topic of trust and we will show why it is necessary to discuss these two concepts as parallel phenomenon. We will end this chapter by presenting how different organizations define the enforcement process and features for an efficient enforcement body.

3.1 Bodies Responsible For Enforcement

3.1.1 The Committee of European Securities Regulators (CESR)

CESR is an independent Committee of European Securities Regulators and was endorsed under the EU Heads of Government Council held at Stockholm in 2001. The Committee was one of two Committees envisaged of the Committee of Wise Men. The report is called the Lamfalussy report (European Commission, 2008) after Alexander Lamfalussy who led the work and the discussion about the European Securities market. The Lamfalussy report recommended a four-step approach for the securities markets, which included:

1. A framework for the EU members with general principles
2. The creation of enforcement committees (e.g. CESR)
3. Means for greater coordination between national regulators of securities market
4. An aim for a better enforcement. (FEE, 2002:15)

The role of CESR is to:

- Improve co-ordination among securities regulators in developing operational network mechanism to enhance enforcement across EU member states.
- Work as an advisory group to the EU Commission concerning issues of securities.
- Ensure more consistent day to day implementation in EU member states. (CESR, 2009).

Each member state of the EU has one member on the committee and is nominated by each member states. CESR released in 2003 (see appendix 4) its "Standard No.1 on Financial Information – Enforcement of Standards on Financial Information in Europe" with 21 principles that would work as a guideline for each member state when setting up a proper enforcement (CESR, 2009).

CESR state in principle number one that the purpose of enforcement of standards on financial information is:

“To protect investors and promote market confidence by contributing to the transparency of financial information relevant to the investors’ decision making process.” (CESR, 2009).

Further principles state that the enforcer shall use a wide spectrum of checking procedures ranging from pure formal checks to in-depth substantive checking. Where a material misstatement is discovered there is a range of possible actions for enforcers to take (e.g. requests for reconciliation or corrective note, restatement, suspension from trading or delisting). The enforcement authority should also have adequate independence from government and market participants, possessing the necessary powers and having sufficient resources (CESR, 2009).

3.2 Swedish Enforcement Bodies FI, Panelen and OMX

3.2.1 Finansinspektionen (FI) and Övervakningspanelen (Panelen)

FI has the authority from the Swedish government as a public authority to create an effective consumer protection and promote stability and efficiency in the Swedish financial system. Their work involves supervision, monitoring and authorization of all companies operating in the Swedish financial markets, more specifically, 3700 companies plus 300 listed companies. FI is the Swedish representative at CESR and requirement from CESR demands that 300 listed companies on OMX and NGM have the responsibility to make sure that information concerning their financial information can be delivered to FI and be reached through out the EU members (FI, 2009).

Before the new law from 2007 “Lag (2007:528) om värdepappersmarknaden” came, the responsibility of the surveillance and enforcement was on the organization Övervakningspanelen (Panelen). Panelen was an independent self regulated organization with a mission to monitor Swedish companies which were listed on a share market and were compelled to make an annual report (Övervakningspanelen, 2006). Panelen made comments when they perceived that companies had not followed existing standards. They did not have any other possibilities to sanction companies so OMX had possibilities to sanction them instead (Norberg & Thorell, 2009:115).

3.2.2 Nasdaq OMX Stockholm AB (OMX)

OMX is today owned by NASDAQ and is the largest exchange company in the world with trading, technology and public service capabilities in six different continents (Nasdaq OMX, 2009). From July 1st 2007 OMX are responsible for enforcement and surveillance of listed companies’ financial reports. The selection of companies for investigation is based on a risk-based approach. OMX investigated 60 companies in 2007 of which 30 of those received a comment letter concerning lack of disclosure. The lack of disclosure was not severe enough for OMX to take any further actions (Nasdaq OMX, 2007).

OMX enforcement methods consist of a read through of the financial reports with exchange of letters with the concerned company. Overall there is a clear lack of guidance on how the surveillance should be done in Sweden apart from the LVPM law according to Norberg and Thorell (2009:116-7). OMX has the authority to delist a company if the violation of the rules is serious and for other cases they can deliver penalties of 15 annual fees. A violation can also consist of a written warning (Aletir, 2008). FI has also the authority to sanction a company which omits to disclose necessary information from a minimum 50 000 SEK to maximum 10 million

SEK. It is therefore OMX that has the primary responsibility for the enforcement of IFRS and its sanctions (Norberg & Thorell, 2009:118).

OMX has been criticized by Arnell & Janzon (2009:6-7) for not interpreting IFRS as they should. They are claiming that OMX are demanding disclosure that does not exist in IFRS and they make assumptions that deviate from IFRIC¹. Further, OMX is acting as a normative body when their actual job is to monitor the listed companies' financial reports. By doing this the OMX is on its way to creating a Swedish GAAP instead of an IFRS GAAP.

There has been a publication from OMX in "Framställan om ändring av lagen (2007:528) om värdepappersmarknaden avseende redovisningstillsyn" saying that they wish not to continue with their surveillance role. They address the following arguments:

1. OMX doesn't have a front edge competence in house and have to hire consultants for the enforcement.
2. To be designated an enforcement role in a competitive environment is strange according to OMX. Only Portugal has the same model of enforcement and this is a disadvantage from a competitive point of view. Sweden should follow the model that exists in the rest of the EU.
3. Last, OMX is not the only market place in Sweden that has duties to enforce IFRS. NGM and maybe soon another market place are on its way. OMX says that there is a need for one organization taking care of the enforcement and not several, to achieve a fair, coordinated and efficient market place.

We will continue this theory section with presenting relevant aspects about trust and how it is relevant and essential for the enforcement process of IFRS. Trust is, as you can read further below, one of the main components when building an effective enforcement system.

¹IFRIC (International Financial Reporting Interpretations Committee) is IASB own interpretation committee (www.iasb.org)

3.3 Trust

As the purpose of enforcement is to prevent and identify errors in the financial statements we find the concept of trust to be an interesting aspect in this thesis. One can always question the efficiency of enforcement, and in this case, if the work in Sweden done by enforcement bodies (FI and OMX) is efficient enough to increase the trust towards the financial statements. We aim to elucidate the trust aspect among creators of financial statements when considering the work of enforcement today done by the enforcement bodies (FI and OMX).

This part of the frame of reference aims towards introducing the concept of trust, its importance in business and the link to control, which we in this thesis relate to enforcement. We find the relation between trust and enforcement strong. This since the creation of trust towards the financial statements through the work with enforcement to should be an important aspect.

3.3.1 Definition of Trust

Trust can be seen as a multilevel phenomena existing in different levels, i.e. at the organizational, personal, and international. Researchers even consider trust to be the key element in successful cooperative relationships (Ring & Van de Ven, 1992:484). Despite this importance of trust, one can find numerous definitions and different perspectives. To begin with, trust can be seen as part of a social organization. The idea of trust as a social relationship is where principals invest resources and authority, to gain a future uncertain return (Baithwaire & Makkai, 1994:625-6). Trust can be explained as the expectations of an organization or individual's trustworthiness in relation to the actions characterized by commitment and behaviour. In other words, if there is a strong trust between A and B, they are expected to fulfil the duties in each other's interests. (Zaheer, McEvily & Perrone 1998:143). Hillebrand, Nooteboom & Woolthuis (2005:814) define trust as:

‘Trust one has in the intentions of a partner towards the relationship’

3.3.2 Importance of Trust in Business

Through the definitions of trust, mentioned above, we now turn to the importance of trust in business today. Due to the past ethical financial scandals, e.g Enron, concerns have been raised towards the accounting and auditing profession today (Copeland, 2005:35). Although the purpose of an auditor's review is to create and ensure an objective view is illustrated in the companies' financial statements, the value of the audit depends upon the stakeholders' values and perceptions about the auditor's work, such as independence and professional judgement (Kerler III & Killough, 2009:111). To regain this trust lost towards the auditing and accounting profession the reputation needs to be rebuilt. To do this, several actions are taken, both by practitioners and in academics (Copeland, 2005:35). One of the actions taken involves increased regulation and governance (Barlaup, Dronen & Stuart, 2009:183). Through this, we find trust to be a critical and important concept today.

The concept of trust has a fundamental meaning for the social order in general, and originates from studies related to social science. Trust has been thoroughly studied by Ramirez, whom also says that only societies, which are based upon mutual and two-way trust between the political side and the general public, are able to persist in the long-term (SOU 2004:78). According to O'Hara (2004:64-5) and Clarke (1999:17-8) trust is a necessity today. Due to the large complexity in the modern world these days, and it requiring large interactions between people, trust is a requirement. Trust between actors may reduce the complexity; as it is possible to allow

interaction and inference beyond obtainable information, create generalised expectations of behaviour, and allowing us to reduce uncertainty. This since there is no need for the whole truth when we trust.

There are two major scientific views on trust; one from the perspective of economics and the second shaped on the basis of culture and its differences. From the first perspective, trust is defined as the construction of social capital and rational actions from agents shaping social entities, which through their cooperation helps build trust (SOU 2004:78). In other words, actors in a society will base their decisions upon a specific set of preferences (O'Hara, 2004:62). These economic contexts are seen as particularly vulnerable as confidence and trust is difficult to sustain. Considering this, participants are often in a position of significant ignorance due to the general technical complexity of exchanged goods and services (Clarke, 1999:17-8). Relationships between actors in a society can be further categorized into vertical and/or horizontal. Vertical relationships, also called hierarchal, involve authority being passed downwards. These relationships may be problematic when considering trust. In this situation the important element of reciprocity is lost. In a vertical relationship, actors are affected by decisions they cannot take themselves (O'Hara, 2004:156).

Studies show that the existence of regulatory institutions is not enough to control actions, there also has to be trust between people, and more importantly, between larger actors acting in the economy. This trust involves the notion of confidence that others follow laws and regulations, and that it is possible to rely on people to follow written and oral agreements. Not only literally, but also relying on people to understand its true underlying meaning. It is the dominance of such attitudes in a society that contribute to the creation of economic growth (SOU 2004:75).

3.3.3 Can the public sector contribute to the creation of trust?

Bo Rothstein, expert in political science at the University of Gothenburg, discusses the public sector and the creation of social capital², with the construction of trust in focus. One can relate trust and social capital to the theory of social pitfall. This theory is about situations where everyone realizes the best solution is to cooperate. However, if one cannot trust that the other partners will collaborate, it becomes pointless to decide for oneself to. If everyone follows the same reasoning, there exists a social pitfall where all end up as losers. In order to prevent these kinds of pitfalls, the solution is trust. In other words, an efficient cooperation is created through the work towards common means, which only can arise through trust (Rothstein, 2003:21-2). It may be a rational decision to not cooperate and the choice of strategy depends upon how one perceives the likelihood of others doing one way or another (Rothstein, 2003:24).

Commonly studies originate from the notion of self-interest and utility maximization. However, this is not a logical foundation when studying the problem of social pitfalls (Bates, 1997:85). Through this, when analysing one should not omit from the unlikely situation where everyone are perfectly informed and strictly rational. Instead one should pay attention to how the political actors today act under incomplete information and with limited knowledge of the actual actors and rules (Rothstein, 2003:26).

² Social capital involves the extent trust and legal security is present in an economy (Eklund, 2007:509).

The theory of social pitfall is important to consider due to two reasons:

1. Actors in a situation where it is possible to decide to cooperate or not, may create a situation that is adverse without intention. This could for example omit from a counterpart interpreting an action as treacherous or threatening and later pay in kind.
2. When an individual, group or organization finds themselves in these kinds of situations it is unfortunately hard to break away. To stop a prolonged social pitfall means that people whom for a long time distrusted each other should almost simultaneously start trusting one another. Trust is a highly psychological phenomenon, and no matter how rational it may be, it is hard to forget something (Rothstein, 2003:30).

Several survey investigations have been made in different countries studying to what extent citizens trust different political institutions and the government. The general, and most common, conclusion from these investigations is that a strong correlation between trust and political institutions does not exist (Rothstein, 2003:173).

Sweden is a typical example, as the trust towards the political and public institutions has reduced in size significantly, while, at the same time, the social trust remains constant. Through this, the trust towards the government, the Parliament, and parliamentary parties can reduce without it affecting how people perceive trust towards other people. However, studies show that the decline in trust towards the political institutions is not equivalent to the trust towards the administrative institutions, such as, the police and daycare institutions. This implies that there is a correlation between trusting more community-oriented institutions and trusting other people (Rothstein, 2003:173-6). Rothstein concludes that it is the extent of impartialness, objectivity, and equal considerations that are the decisive aspects when it comes to the creation of trust towards political institutions (Rothstein, 2003:197).

“Trust, both considering toward individuals and institutions, is hard to earn but easy to destroy” (Rothstein, 2003:199).

3.3.4 Two Dimensions of Trust

Das & Teng (2001:255-7) also discuss trust through two dimensions; competence trust and goodwill trust and involves the positive expectations related to these. The first dimension corresponds to the expertise, ability and technical competence. This is based on the various resources available and the capabilities. Goodwill trust, on the other hand, relates to the responsibility, intentions, integrity and moral obligations. Nooteboom (1996:990) explains these two broad notions of trust as:

‘Trust may concern a partner’s ability to perform according to agreements (competence trust), or his intentions to do so (goodwill trust)’.

Competence trust refers to technical, human, operational and financial abilities. These kinds of trust developed skills are needed to perform a task. Further, it is also developed based on the level of search undertaken to gather the skills necessary and trying to find the right people for the task. Further, it is more likely for a party to engage in a collaborative relationship if they perceive that the other party/parties are capable in performing their tasks (Paul & McDaniel, 2004:187).

A lack of trust in the controller-controllee relationship may create a questioning of competence to the controller. An insufficient goodwill trust could make controllees question of the controller pursue private interests instead of acting upon the common and mutual interests. Further, a lack of competence trust could make controllees wonder whether control is really the solution (Das & Teng, 2001:265).

3.3.5 Trust and Control

‘The essential character of all trust relations is their reciprocal nature. Trust tends to evoke trust, distrust to evoke distrust As trust shrinks, distrust takes over ... differing degrees of trust are perceived as being embodied in the rules, roles, and relations which some men impose on, or seek to get accepted by, others’ (Fox, 1974: 67–8).

Control is often associated to harm trust because regulation may create a sense of mistrust. However, in opposite, some researchers claim that appropriate control tools and procedures might create trust as it can function as a ‘track record’ helping people to justify whether they do their jobs well or not. Trust could reduce the level of resistance and create a balance in the controller-controllee relationship (Das & Teng, 2001:263-5).

Today there is a focus of trying to sustain trust between actors through regulation. Trust needs to be maintained on a regular basis, and this is a common feature of regulatory relationships. A successful regulation and a legitimate compliance must be represented by a mutual trust between the regulatee (the auditors and the companies) and the regulator (the enforcement bodies). This involves actions that are appropriate and necessary by the regulator, as well as, from the regulatee’s perspective, there should not be abuse of trust by actively not following agreed standards (Clarke, 1999:25,146). Furthermore, the concept of trust is also interesting to discuss using the relationship between expert and advisee, which more or less can be related to the one between the regulatee and the regulator. In this aspect, the advisees generally lack the expertise needed to evaluate the experts’ performance. This is a problematic issue. As expertise is supposed to provide intellectual labour and represent a conservation of important resources, this idea is defeated if experts cannot be trusted, as we somehow need to become experts ourselves instead (O’Hara, 2004:161).

Rothstein (2003:291) discuss the importance of social capital, especially when trying to give the impression of trustworthiness. The importance of trust in the society is important today due to:

“ Trust above all, as it keep our senses open for all support, ensure communication and dialogue”

Rothstein also emphasizes the importance and essential part, regarding trust, that actors with conflicting interests should be able to create universal and neutral set of rules and regulations. To achieve this, actors participating in the discussion have to have trust towards each other’s interests and that their speaking is frank.

Regulation is not enough to create trust, as discussed in section 3.1.2 *Importance of Trust in Business*. There also has to be a risk of being caught when undertaking incorrect actions, and, through this, become sanctioned. It is all about creating a balance in the triangle of trust. On top of the triangle of trust, as shown below in Figure 6 *Triangular Approach to the Creation of Trust* are the norms. These are what control individuals, companies, and organizations today. In order to achieve a high level of trust, the written, as well as the unwritten, set of rules and regulations should be perceived as clear, relevant

and in accordance with the values within the area of interest. However, without a risk of being caught, a good set of rules and regulation leads nowhere. (SOU, 2004:153).

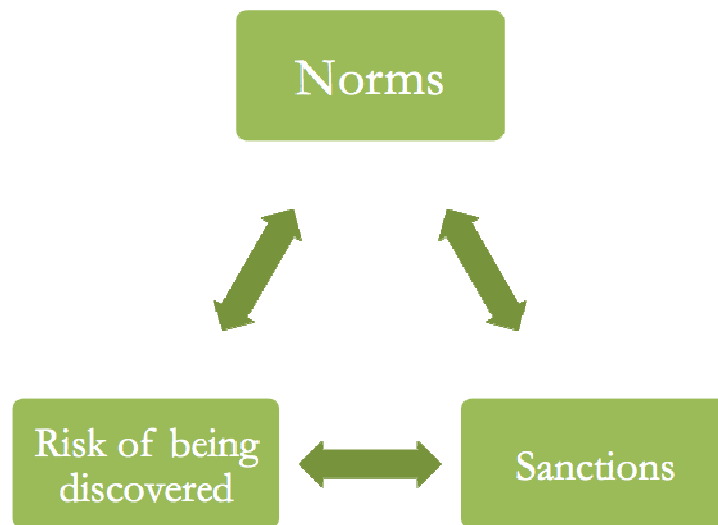


Figure 5 Triangular Approach to the Creation of Trust (SOU, 2004:153)

If the risk of being discovered is low, the probability of following rules and regulations is low. A clear example of this is speed restrictions. If one is unlikely to get caught by police while breaking a speed limit, the likelihood of doing it is high. The risk of being discovered can also be related to social control and surveillance by mass mediums. In spite of this, if the sanctions are low or insignificant it is not enough with a good set of rules and high risk of being discovered. Through this, the size and impact of sanctions play an equally important role in the creation of trust. To summarize, the triangle of trust needs to be in balance in order to create trust. It is not enough if two corners are well formulated if the third one falls short (SOU, 2004:153-4).

In the last section of this chapter we are focusing on definitions of enforcement and what EU and other organizations have written about it. You will see that enforcement appears in more than one level and can be divided into different categories. Further, the FEE organization has given nine features for an effective enforcement body that we will present.

3.4 Enforcement Mechanisms at Different Levels

In the article "EU Financial Reporting Strategy: the way forward" from 2000 the EU Commission is expressing its will that all EU listed companies listed on a regulated market should be required to prepare consolidated accounts according with IAS. The IAS standard will according to the Commission increase comparability in the financial reporting and will greatly simplify the enforcement mechanism. The EU Commission describes enforcement of accounting standards as (2000:4):

"a cascade of different elements including (1) clear accounting standards (2) timely interpretations and implementation guidance, (3) statutory audit, (4) monitoring by supervisors and (5) effective sanctions. Each of these must work efficiently: the system will be as strong as its weakest part in delivering strong investor and creditor protection."

The above report states that enforcement appears in most of the European countries at six levels:

1. **Self-enforcement: Preparation of Financial Statements**
The responsibility lies at the management of the company. They should have sound corporate governance in place safeguarding the implementation of accounting standards.
2. **Statutory audit**
The audit is an important part of the financial reporting because it subjects information to independent and objective scrutiny. Trustworthiness and effectiveness are vital to an effective allocation of resources in the capital market.
3. **Approval of financial statements**
Approval exists in all countries in some way. The most common place to approve the financial information is at the annual general meeting (AGM).
4. **Institutional oversight system**
This contributes to the effective enforcement of accounting standards. The institutional oversight system differs from country to country. It will be discussed and presented in next section.
5. **Legal sanctions and complaints**
In all countries there exists a system of sanctions via civil or criminal procedures.
6. **Public and press reaction**
The risk of reaction from the press and the public should not be underestimated. Naming and shaming may play an important role in the enforcement process.

3.5 Different Enforcement Bodies in Europe

Enforcement of financial reporting rules can be handled by different sorts of bodies. These include:

- Stock exchanges; (e.g. Norway, Sweden and Switzerland)
- Regulators of stock exchanges; (e.g. US, Australia, Belgium, France, Italy)
- Government departments and agencies; (e.g. Denmark and Czech Republic)
- Private-sector bodies. (e.g. UK)"

There is not an ideal model of an enforcement body that will fit all countries according to Nobes and Parker (2006:175). The sort of body to be chosen is dependent on what kind of regulatory system of the country's culture and more specific its political, legal and financial system which changes over time. Two of the most historically effective bodies are the SEC in the US and the FRRP, Financial Reporting Review Panel.

The case for many countries until recently was that the annual audit was the only monitoring mechanism. This is a necessary component but it is unlikely to be sufficient. Auditors are perceived to have difficulties to maintain their independence. Auditors can benefit from the enforcement bodies work since the auditors' only means of enforcing compliance with IFRS standards is to qualify their audit opinion. Enforcement bodies can also benefit from auditors

because enforcement bodies cannot check accounting records in detail and therefore rely on the work of external auditors in this respect. The existence of enforcement bodies strengthens the ability of the auditors to insist in compliance with financial reporting standards (Nobes & Parker, 2006:175-6).

As stated above there are many different solutions to implement the enforcement. One can ask why there is not one single European enforcement body or a European SEC? Ideally, a global standard like IFRS should require a global enforcement. However, to make the enforcement as effective as possible it needs to have access to a court of law which would have worldwide jurisdiction. A single European enforcement would not only need a Treaty but would also require a higher degree of harmonized securities regulation than that is currently available today (FEE 2002:18). This is of significant challenge, not only the challenge of trying to establish equal enforcement standards but also to manage all the different types of enforcement bodies (Brown & Tarca 2005:182).

3.6 Essential Features for an Effective Enforcement Body

The Fédération des Experts Comptables Européens (FEE) made in 2002 a suggestion on how national enforcement bodies should prepare themselves in order to identify essential features of an effective body; those included:

1. Support for high quality corporate governance and external audit

Effective enforcement relies upon all those with influence on financial reporting playing their part. It is important that the enforcement body supports the audit function via discussion of financial reporting issues between companies and enforcement bodies should take place in the presence of the auditors, and on the basis of a comprehensive written explanation of the issue confirmed by the company's Board.

2. High quality, expert, globally-consistent decisions on important issues

IFRS needs to be applied rigorously and consistently to all companies throughout Europe, with due regard for how they are applied elsewhere in the world.

3. Freedom from bias

The enforcement body should make unbiased decisions. Individuals working with enforcement should avoid conflicts of interest arising in individual cases.

4. Transparency and clear procedures

Transparency of the activities of the enforcement body is of crucial importance for widespread acceptance of their decisions. Enforcement bodies should demonstrate that they follow clear procedures and take enforcement decisions in a competent manner.

To ensure transparency of decisions stating where financial information has been found by the enforcement body to be defective and is to be corrected, there should be a clear, well known and public statement that is widely disseminated.

Enforcement bodies should feed their decisions to IASB or IFRIC. These decisions should also be referred to EFRAG.

5. **Confidentiality and speed of action**

Errors and omissions may lead to the creation of a false market in shares or debt instruments. Once an issue has been identified as noncompliance, it is important that it is resolved quickly, so that appropriate information can be shared with market participants as soon as possible.

6. **Avoidance of making detailed accounting rules**

It remains vital that accounting standards be based on principles and not detailed rules. Rules could enter the IFRS environment within the text of individual standards or interpretations, or by many different enforcement bodies publishing their own positions on how the various principles should be applied. Enforcement bodies should refer problem interpretation issues to the IASB and IFRIC as well as to EFRAG.

7. **Focusing resources**

A risk-based approach should be considered in determining the scope and coverage of reviews to allow for efficient allocation of enforcement resources.

To prevent waste, procedures should be in place to avoid time consuming and expensive investigations of relatively minor matters of non-compliance and to identify malicious, trivial or ill-informed complaints.

8. **Rectification of defective financial information**

The proper rectification of defective financial information is a characteristic of good enforcement. The appropriate means of rectification depends on the particular case and could range from restatement of defective financial statements to subsequent disclosures or other forms of publication.

An enforcement body needs to have the power to start a court case and sufficient financial resources to do so, to defend its decisions and to appeal against adverse court rulings.

9. **Sanctions**

In order to ensure that enforcement decisions and rectification are implemented, a proper sanctioning system for all responsible parties involved is essential. It is not a necessary feature of an enforcement body that it should itself become involved in imposing sanctions. There are strong arguments for separating the role of enforcing correct application of accounting standards from the additional function of sanctioning. The primary emphasis of an enforcement body should be on correcting inappropriate application of IFRS, so that the integrity of financial information is upheld.

3.7 Chapter Summary

This chapter has given an overall insight into the work of enforcement in Sweden today and the responsible enforcement bodies (CESR, FI and OMX) to enhance the understanding for the problem in this thesis. Further, the concept of trust can be seen as a multilevel phenomena existing at different levels, and we find trust to be a critical and important concept. O'Hara (2004:64-5) and Clarke (1999:17-8) specifically state that trust is a necessity today. Studies show that the existence of regulatory institutions is not enough to control actions, there also has to be trust between people, and more importantly, between larger actors acting in the economy (SOU,

2004:75). Das & Teng (2001:255-7) also discuss trust through two dimensions; competence trust and goodwill trust, and narrate the positive expectations related to these. The first dimension corresponds to the expertise, ability and technical competence. This is based on the various resources available and the capabilities. Goodwill trust, on the other hand, relates to the responsibility, intentions, integrity and moral obligations.

Moreover, a section related to social capital and the theory of social pitfall, discussed by Rothstein (2003:24), is included which emphasizes the importance of cooperation in order to create trust, and the obstacles involved when finding oneself in a social pitfall. As mentioned earlier in this thesis, we relate trust to enforcement from the aspect of efficiency. More specifically, in relation to how efficient the surveillance conducted by the enforcement bodies is, and if it increases the trust towards the financial statements. As the purpose of enforcement is to prevent and identify errors in the financial statements, one can question the procedures and the impact. Finally, we learned in the last section about E U's view and what other organizations have written about enforcement. Further, the FEE organization gave us a tool consisting of nine features for an effective enforcement body that will be useful for answering our purpose.

The next chapter will present the empirical findings from the interviews conducted with representatives from five larger listed companies in Sweden, the four largest auditing firms, and OMX, as well as, FI.

4.

Empirical Findings

In this chapter we aim to present the answers from our interviews. The respondents consist of five large listed companies, the big four audit companies plus FI and OMX. The interview questions have the same construction for the listed and the audit companies (see Appendix 1) however, the interview questions to FI and OMX were somewhat modified (see Appendix 2-3). The first part of chapter four Empirical Findings, corresponds to the major part, to research question one, and the second part to research question two, as far as it is possible. Therefore we find the answers to somewhat overlap the two research questions.

4.1 Opinions about the Enforcement Bodies' Surveillance

One of the research questions, specified in chapter one *Background*, relates to the opinions about a fundamental need for the surveillance agencies work with enforcement.

- How is FI and OMX's work perceived today by attesters and preparers? Is there room for improvement or a need for it in general and if so, why?

It is well known that auditors have a fundamental responsibility to ensure the credibility and trust for the financial information, but what about the credibility that the Swedish enforcement agency brings? This first part in this chapter aims towards explaining the respondents' interpretation of the purpose and need, as well as the possibility of actually discovering mistakes and faults in the financial statements through the surveillance from the enforcement bodies (FI and OMX) in Sweden today. We found it interesting to also find out whether the respondents' view and interpretation of infringement in general differs and how they perceive sanctions. This is worthy of note since it may affect how the respondents perceive a possible sanction and how they, in turn, and in between the lines, recognize the risk and seriousness of the work of enforcers.

4.1.1 The Purpose and Need of Enforcement Bodies

To summarise the opinions related to the work of FI and OMX, all of the preparers (the companies) seem to agree that, compared to the earlier situation, the idea of surveillance today is better. As two of them chose to express it:

"There was definitely a need for a change in the old organization. It was very specific, and people from the larger auditing firms conducted the surveillance. Everything became highly specific and detailed. There was a need for a harmonization with people representing companies too."

“An efficient capital market needs surveillance. However, I doubt that FI has the competence necessary, and who is responsible today?”

One of the five preparers (the companies) also chose to relate the subject to the case in United States, where the work of SEC is found as necessary. To retain the trust lost from several scandals, the work of an independent party is important. The preparers also specifically say that there is always a risk for auditors to become blind to flaws, which in some cases has also been proven due to the actual findings from the enforcement bodies.

The four attesters (the auditors), on the other hand, differ somewhat in their opinions, in comparison to the preparers (the companies). Two still find it hard to tell if a need exists, while one of the remaining attesters says that there was a need to change, and the other attester says no. However, they all mention “Panelen”, which was operating before the law of LVPM. The attesters (the auditors) perceived this organization to be very good, but understand that it was hard to maintain in a globalised milieu.

When considering the opinions of the enforcement bodies (FI and OMX) in relation to the need for a change of enforcement, there was not a clear need for a change since the rules and regulations today would have made it possible for the Panelen to survive, according to FI. Furthermore, FI said that OMX were able to outsource the surveillance to Panelen, if they wanted to. OMX, on the other hand, found that there was a need for a change. This since one was forced to have a discussion about how the laws should be interpreted, which forced the surveillance to be more formal and regulated treatment.

Another aspect drawn to attention through the interviews is that the preparers (the companies) seem to be confused about who is actually performing the surveillance, is it FI and OMX? One of them chose to explain it like this (Börsen is used synonymously with OMX):

“At first, I believe, the purpose was to let Finansinspektionen do it, but then Börsen was appointed instead, and now I’m unsure who is actually responsible. I have heard something about Finansinspektionen, if I have interpreted the debate correctly. It is a kind of vacuum, and I’m unsure if Börsen has hired people from the large auditing firms to do the surveillance for them”.

When allowing the respondents to explain their interpretation and idea of the purpose with the enforcement and surveillance today, the answers differ significantly. To begin with, some of the preparers (the companies) view the work of surveillance today as a way of getting a “second opinion”, and assuring that the current standards and regulations are undertaken properly. However, there are also preparers (the companies) stating clearly that the purpose is unclear, and:

“I don’t know, highly unclear. The directive from the Finansinspektionen is unclear.”

The attesters (the auditors) more or less agree that the purpose of the surveillance today is to monitor and control that accurate directives are complied with and to guarantee a correct national, and international, accounting. Sweden has to stand a comparison at an international level. Through this process, the role of the auditors will indirectly be strengthened.

The enforcement bodies (FI and OMX) describe the purpose of the enforcement to be a direct translation of CESR’s standard no. 1. The purpose is about creating an effective capital market, and be able to protect investors through somewhat standardized accounting. FI continues and says:

“The main purpose is not to punish the ones doing wrong; it is about creating a high quality of its application. One can also relate the purpose of the enforcement to trust.”

4.1.2 Possibilities to Discover Material Errors

The possibility for FI and OMX to discover material errors³ is, according to all preparers and the attesters, difficult. Both preparers and attesters find that if someone should be able to discover deviations it is the auditors, due to the fact that their resources are significantly larger. Several also specify their answers by saying that the enforcement bodies only have the possibility to review on the surface, which in turn will not create a deeper understanding for the companies' business and the required considerations done. One of the attesters interprets and explains their work as follows:

"They sit and read annual reports, they would do more good through investigations on spot, but they don't. Through these they would be able to discover a lot more. However, from the annual reports they are able to get an indication. To conclude, they are able to do more efficient work but omit to do it. They seem pleased after their desk-top reviews."

Another interesting aspect is that the knowledge about cases actually discovered by FI and OMX differ between both preparers and attesters. When considering the preparers, about half of them had knowledge about specific companies that had been under investigation. However, the others had less knowledge, and in one case none about any cases. The attesters, on the other hand, knew more about specific cases than what the preparers did, in general. However, one of the attesters thought of OMX's work:

"Is Börsen transparent with their information? No, they are not. A review of an interim financial report is not made public, one does not hear anything directly about any investigations; I demand more public reviews and comments. It is hard to find any information about what is going on and happening."

FI did not specifically want to say anything about the possibilities for OMX specifically to discover material errors. However, they said that an enforcement organization in general has the possibility to discover infringements. But whether the enforcement organization succeeds or not is another issue. OMX, on the other hand, said:

"As you understand no, the possibilities are small. One may discover obvious errors regarding disclosure requirement. But if one should add the valuation part one has to go deeper into the accounting procedures to see whether it is correct or not. It would only be discovered if the companies made a larger error. What one might find is the interpretations and judgements in the grey zone."

4.1.3 Definitions of Infringement

All respondents seem to agree that an infringement can be defined as an incorrect judgement, where the requirements for information and transparency are not fulfilled. Further, some of the respondents use the word "essentialness", and clarify that a detailed and too specific surveillance should not be the primary objective. One should bear in mind the level of complexity in IFRS, and the numerous considerations companies and auditors are forced to do.

Furthermore, we asked the respondents to separate a clear and unclear infringement. In general, a clear infringement is when a person/company/stakeholder, due to unclear and wrong

³ "The information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statement" according to IASB Framework paragraph 30.

information, depicts incorrect conclusions based on the financial statements. One of the respondents is more specific and says that a clear infringement is:

“When the assets are valued high and liabilities are valued low”

An unclear infringement, on the other hand, seems to be the unclear difference between what companies owe and should disclose in the financial statements, and what is actually unnecessary. As one of the respondents choose to explain it:

“To, for example, follow all details in IAS 39 is not reasonable. There is a grey zone when it comes to company secrets and what to protect. Some information requirements from IFRS states that companies in general today give more information than what is necessary”

4.1.4 When is it Justified to Take Action, and is it Even Possible to Sanction?

The work done by OMX is difficult and by using a rather principle based standard as a base does not make the task easier, according to some respondents. The level of subjectivity is higher than it is when interpreting the US GAAP. IFRS are becoming more complex and voluminous and one of the respondents is giving IFRS 39, about financial instruments, as a returning example.

All of the respondents use the word ‘significant’ when describing the justification for OMX and FI to take action. They say that it is only when the infraction and non-compliance is of significant character OMX and FI should remark and observe, and as a second step possibly sanction.

When considering what and when to sanction, one of the preparers choose to express this:

“All significant infractions and non-compliances should be sanctioned. If one does not use sanctions it is hard to know what rules to follow. The compliance of IFRS is hard, and practice and there are many detailed recommendations, so from there to practice is a large step. Different kinds of forums are used to establish correct interpretations, and I don’t find Börsen or FI to have the competence needed in these situations. It is a difficult area of subject. There is always a grey zone, much due to the high demands on the information, in comparison with unlisted companies. Börsen and FI do not have the competence to utter whether it is correct or not.”

This statement suggests that FI and OMX do not have sufficient competence to actually sanction all non-compliances. This since, according to this preparer they do not have enough knowledge and insight. The concept of trust is further evaluated in the next section.

We also asked how the respondents interpreted the issues of sanctioning a system that is principle-based, and are there any issues? Unfortunately, we find this question hard to code as the answers differ considerably. However, the attesters answered somewhat similar as they all said that a principle based system is preferable and entails more professional judgments. Due to this, it is harder to sanction and calls for a deeper understanding of the actual adjustments made in particular cases.

The preparers, on the other hand, discussed this topic more freely, and two of them said:

“A principle-based system gives opportunities for interpretations, and one has to investigate more as an external reader than only the annual report. Depending on how material the information is in relation to the group in general, where should one draw the line? There will always be difficulties of this kind.”

“Harder to say if something is highly wrong and harder to investigate specific details. However, in the rules-based milieu it is hard to be concrete, legible and treat all cases

similar, which means loose outlines even though the grain is the same. This put higher demands on the enforcement and involves more judgments.”

The enforcement bodies both reasoned around the fact that it is not hard to identify the errors, just because it is principle-based, however to sanction is a lot more complicated. No matter how clear and well formulated a principle, or rule is there will always be different interpretations and exceptions. They also mentioned that as an enforcement organization you are not allowed to issue interpretations, since these are supposed to only be issued by IFRIC. OMX continued the discussion and said:

“The problems with a principle-based system are the estimation part in the financial reports. This is where the companies themselves decide the valuations. All entries that are of significance almost always originate from estimations and affect the financial statement. It is hard to question these. One can discuss these with the companies but in the end it is hard to tell whether it is right or wrong. What is interesting here is the surveillance, where it is about judgments and the analytical skills. There are large scales of freedom in the system today and these types of questions put pressure on companies. One should not think that just because no errors are found everything is correct.”

4.2 Aspect of Trust

As shown and explained in chapter one *Background*, we have a specific research question related to the aspect of trust. The concept of trust has a fundamental meaning and it is important that a successful regulation and a legitimate compliance must be represented by a mutual trust between all parts involved. Trust in this thesis can be discussed at two levels; trust between the enforcers of financial reports (the enforcement bodies FI and OMX) vis-à-vis the preparers of financial reports (the companies) and trust between enforcers of financial information (the enforcement bodies FI and OMX) and attesters (the auditors) of financial information. This leads us to the question:

- Is there a trust from the preparers and attesters for the work with enforcement of IFRS today done by FI and OMX and if so, how is it expressed?

4.2.1 Trust as a Phenomenon

Trust is a central concept in this sense, and the perception and interpretation of the concept is important. To summarize, trust according to the preparers and the attesters is when a counterpart is keeping its promises and does what is agreed. Furthermore, trust is the key to a sound financial system and, as one respondent puts it:

“It is crucial that parts which are involved in the financial process can be trusted and are as transparent as possible. Just the rumor of someone that is acting in an incorrect way can damage the trust and soundness of the financial reports”

The perception of trust between all respondents is somewhat similar and can be further summarized into three words; clearness, consequence, and mutual understanding. What differed between the answers though was the enforcement bodies use of actual juridical definitions almost read from the law-code.

4.2.2 Trust to the Financial Statements

When considering the effect of surveillance in this sense from the enforcement bodies, there is an overall opinion that it contributes to a somewhat increase in trust of the financial statements today. However, the possibility and ability of it to grow even stronger is emphasized. Despite this, one of the preparers under investigation differs significantly in their perception regarding whether there is an increase in trust or not.

“No, I believe there is not. The relation between FI and Börsen is unclear, and the mandate from the department is vague. However, of course there should be a surveillance but with clear missions”

One of the attesters chose to express this:

“A piece of a puzzle, among several others. In the future I believe this piece of puzzle will be easier to tolerate. To create trust is always good. Self-regulation has its advantages in the environment we have today, I find this good. To finance through authorities creates someone actually stirring the pot once a in a while, and forcing people and companies to actually act according to the regulations.”

The enforcement bodies are somewhat uncertain to whether their work actually contributes to an increased confidence towards the financial statements. However, they agree that it should be the case. OMX further defines how it contributes to an increase in trust, and explains that it is the actual knowledge of someone investigating and reviewing the financial reports, which strengthens the credibility. As companies are aware of this review they are probably more unwilling to differentiate too much, and become too creative with their accounting. Despite this, OMX still finds it hard to actually discover errors and says that the auditor is the only one who will discover material errors is the auditor.

4.2.3 Trust to the FI and OMX

The preparers and the attesters have an overall trust for FI and OMX work, or at least its ambition to enforce the IFRS standards. However, almost all are questioning the competence at OMX. The questioning is not just on an individual level, it is a resource-based question as well. As one puts it:

“OMX’s duty in the financial stability is important and sometimes I doubt their skills and competence in the people. It’s seems like they don’t have time for these kind of activities and there are too few people for monitoring it in a proper way”

Others follow the same reasoning:

“Sometimes it feels we know more than Börsen do. They were feeling obligated to respond to our request and gave us an answer that felt simple. It felt that we were not on the same level.”

“I trust their ambitions. I do not trust their overall competence; however, this is related to the lack of transparency. The level of education is irregular sometimes between us and Börsen. More specifically about the competence at Börsen is that it has been a bit floppy between Börsen and FI, and the cases between company X and Börsen have not involved a sufficient level competence according to us. “

One of the preparers elaborates further and discusses that it all comes down to creating a trust towards the attesters that they are performing their job accurately. Otherwise this kind of supervision is about controlling the auditors alone. If there should be a control of this kind, in order to make it efficient, the level and quality of the surveillance needs to be higher than today.

OMX said that they are not interested in having the surveillance due to NGM and maybe other stock exchanges will also share the duty. Others take care of the surveillance, which they pay for. OMX themselves does not possess the competence needed. During the interviews it became clear to us that this surveillance is financed by OMX themselves- not by any governmental funding. In other words, they are paying the experts needed during the investigations. OMX said:

“Övervakningspanelen is the most suitable for this job. They had the juridical competence. Although we use expertise today, they were an independent organization. I believe they would have made a great job today. The best solution to the enforcement today would have been to make use of external experts.”

4.3 OMX as the Organization Responsible for the Oversight

On top of these questions, we asked the respondents how they interpreted the situation today where OMX act as an enforcement body and have in some cases made suggestions based on their interpretations as well.

“No, they shall not act as both. They shall not think so much. Highly ungrounded statements, unkind attitude, you can read for yourselves in their financial statements from 2007. When they do not have reason for what they are saying, and that they should stop doing these sorts of statements. What happened when Börsen comments upon something? They send a letter to the companies, however, it feels as if they close the case pretty fast, probably they don't have enough resources to follow through with it.”

“It is unfortunate that Börsen and FI have made statements that are not in line with CESR and IFRIC.”

Furthermore, some of the preparers are reasoning around the fact that there is a profit-driven company handling the oversight, and find this highly inappropriate.

“Why OMX as a profit-driven company have this responsibility is for me very unclear. I haven't seen this kind of constellation somewhere else”

During the interview OMX told us the difficulties they found with being the organization responsible for the oversight.

“That it is difficult being an enforcement organization due to the situation in-between different interest groups. Auditors are on one side and the authorities on the other. It is difficult to achieve some kind of balance. The second difficulty is the subjectivity of IFRS. Partly through the design and the rules of importance. There is a clear difference between the interpretations of authorities and companies. Furthermore, the size of IFRS, makes it almost unreadable. One cannot take in that amount of information.”

They also said that they found their role in the enforcement process to be a kind of catch 22. Although the intention is not to make judgments and interpretations, it is almost impossible not to in a principle-based system. Earlier, when they were not legally bound to the surveillance they were able to have more opinions.

One of the questions to the enforcement bodies was about what they would change in the enforcement system today in order to make it more efficient. FI wanted to have one organization, and in the end if this is FI or not, it doesn't matter. OMX had three specific suggestions on how to improve:

“Today there is a misallocation between reviewed information and other. A lot of resources are put towards information already reviewed by auditors. One should not forget the other information companies are spreading, e.g. on their homepages which

also affect the stock values. Secondly, the work with standardization is hard due to the amount of subjective interpretations. This in turn does not enable comparability. This has to be changed in some way. And at last, a reasonable surveillance is required. There should be some kind of trace dog reporting to FI. This trace dog is close to the market and is able to see any irregularities. FI as an authority are then able to perform a deeper and more thorough investigation of companies if they find it necessary.”

4.4 Chapter Summary

This chapter has demonstrated the findings from the interviews conducted with five larger listed companies in Sweden, the four largest auditing firms, and OMX, as well as, FI. The presentation is according to the two research questions, as far as it has been possible. Further, the answers were coded through a process of putting likeminded pieces together, and complement deviant answers with quotations.

In the next coming chapter the discussion about the empirical findings is presented. Here the empirical findings are discussed in relation to the earlier chapters in order to answer the purpose of the thesis.

5.

Discussion about the Empirical Findings

Chapter five, Discussion about the Empirical Findings, will guide you through a discussion where we interpret our empirical findings with help from the frame of reference. With guidance from the research questions and the purpose we aim to suggest in the following chapter how the enforcement bodies (FI and OMX) can build better trust towards the financial statements. As mentioned in our method, the benchmark for what is good enforcement is what preparers (the companies), the attesters (the auditors) and what FEE consider it to be. As a reminder from chapter two, our overview of data collection and scope will start this chapter.

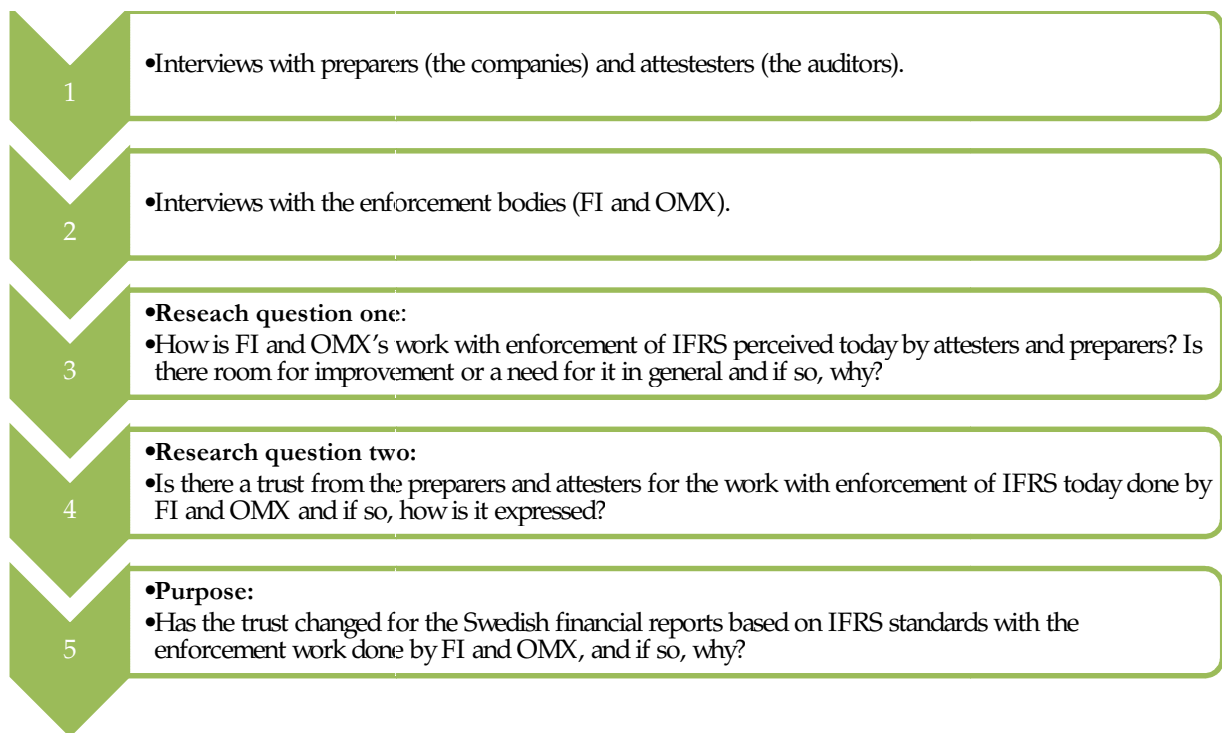


Figure 1 Overview of Data Collection and Scope

5.1 Research Question One

How is FI and OMX's work with enforcement of IFRS perceived today by attesters and preparers? Is there room for improvement or a need for it in general and if so, why?

5.1.1 How Transparent are the Enforcement Bodies FI and OMX with Their Work?

As an introductory discussion to this question, we would like to emphasize that the knowledge about the relation between FI and OMX from preparers and the attesters is weak. One can argue that it is a lack of transparency from FI and OMX or the lack of willingness from the companies and auditors to know how the enforcement is organized.

The amount of information you are able to find on either FI or OMX homepage about the structure is, according to us, not sufficient. Throughout this thesis, one of the key challenges has been to actually grasp this relationship and it is not with surprise we found the respondents to also be somewhat confused about this. When discussing this problem with the respondents from FI, they argue that if you really want to find the information, you can always find it in some way. One can ask if this really is the right way to tackle the situation. Who wants to spend time searching for information and maybe not find it in the end anyway?

We relate this issue to FEE's features for efficient enforcement number four (Transparency and clear procedures) and ask if FI and OMX really accomplish the suggestion about transparency and clear procedures. As several preparers stated, they are not sure whether OMX is involved at all anymore in the enforcement and surveillance or who is actually in charge. After one and a half years, the preparers should be knowledgeable about who is responsible for the enforcement in Sweden, according to us. It is relevant to relate this to FEE's suggestion about transparency, where a general lack of knowledge may create a lack of respect and acceptance to the decisions taken. One of the attesters said (Börsen is used synonymously with OMX):

"Is Börsen transparent with their information? No, they are not. A review of an interim financial report is not made public; one does not hear anything directly about any investigations. I demand more public reviews and comments. It is hard to find any information about what is going on and happening."

When allowing the respondents to explain their interpretation and idea of the purpose with the enforcement and surveillance from FI and OMX today, the answers differ significantly. Although the attesters seem to agree, it is still interesting to discuss the lack of understanding among the preparers. As one chose to describe it:

"I don't know, highly unclear. The directive from Finansinspektionen on what Börsen shall do is unclear."

One of the enforcement bodies had noticed this lack of knowledge and referred to it as a disinterest towards the work with enforcement in general. They do not believe it is only a reason of too few channels for information. However, we find this reaction towards the enforcement bodies and their work to be a result of lack of transparency. Again, as FEE suggestion number four (Transparency and clear procedures) states, in order to achieve an effective enforcement body and widespread acceptance for decisions there has to be transparency in all procedures. We find the lack of transparency as a more intuitive and logical explanation to the lack of understanding among preparers, than a disinterest. We did not find any signs of disinterest towards the work in general, which says the opposite to what one of the respondents from the enforcement bodies said.

5.1.2 FI and OMX Versus Övervakningspanelen (Panelen)

All of the preparers more or less agree that the harmonization of European enforcement is better, compared to the situation earlier with the Swedish self-regulated model with Panelen described in section 3.1.2 *Swedish Enforcement Bodies FI, Panelen and OMX*. We find this to be related to how it actually was performed earlier and the part where companies were publicly exposed in an annual publication about listed companies and investigations in their annual reports and use of IFRS. Pursuant to our respondents, Panelen consisted of knowledgeable people but was too detailed in their opinions sometime.

As the enforcement today has not achieved the same obvious impact according to the attesters and preparers, it may be the answer to why this new system is more favoured by preparers. Since this, there is not the same kind of public humiliation, as one can explain the work of Panelen to be. We would also like to emphasize that all attesters mentioned Panelen and perceived their work and competence as good. However, it is interesting that the preparers specifically say it is better today although all attesters and preparers, but one, hardly have noticed the work of FI and OMX, on top of the confusion discussed earlier in this section. What do the preparers base these opinions upon? Is it because they have hardly been investigated at all, and through this find a somewhat unseen surveillance better? Due to the lack of impact from FI and OMX in their enforcement work, as we would express it, this work is probably more preferred by the preparers due to this.

5.1.3 The Consequences of a Principle based Standard

IFRS is perceived as a principle based standard according to Benston (2006) and Zeff (2007) and the growing length of guidance in the standard has made IFRS more voluminous. One reason for this, according to us, is the problem of enforcing a standard that is based more on principles and has more subjective alternatives than for example US GAAP. This assumption was supported by the respondent from OMX when he mentioned all the “grey zones” that you could find in IFRS. The question of what is correct and what is wrong according the IFRS principles is sometimes very hard to define he continued.

“IFRS is detailed in many questions and it is looking more as a rules-based standard. Unhesitatingly, IFRS is moving towards what US GAAP is today.”

Another issue that was linked to the interview question of principles versus rules standards was if OMX should work as a normative body and not only as an interpretive body. The whole idea with the work of CESR is to make sure that member states in the EU are using CESR’s “Standard No.1 on Financial Information – Enforcement of Standards on Financial Information in Europe” (see appendix 4) and not interpret the standard and become normative. OMX was criticized by Arnell and Janzon (2009:67) when they claimed that OMX had made disclosure that doesn’t exist and interpretation that deviates from IFRIC⁴. All respondents agree that OMX and also FI should not act as a normative body but the respondent from OMX said that it is more or less impossible not to make interpretations of IFRS because the way it is structured. There are “grey zones” where you can’t find a proper answer and that is why we have interpreted the

⁴ IFRIC (International Financial Reporting Interpretations Committee) is IASB own interpretation committee (www.iasb.org)

standards that deviate from IFRS and IFRIC. It is unfortunate if someone has perceived this as being a normative attempt he continues.

CESR is the responsible organization for the enforcement in Europe and all listed companies should follow IFRS. FEE has warned about enforcement bodies publishing their own position about how the various principles should be applied. It is important according to FEE's suggestion on efficient enforcement number two (High quality, expert, globally-consistent decisions on important issues) that IFRS is applied rigorously and consistently to all companies in Europe. This suggestion is linked to FEE's suggestion number six (Avoidance of making detailed accounting rules) about publishing own positions about principles that are not in line with IFRS and IFRIC.

Again, OMX pointed at the difficulties they found with being the organization responsible for the oversight and compared it to a catch 22. Although the intention is not to make judgements and interpretations, it is almost impossible not to in a principle based system. Before the LVPM, when they were not legally bound to the surveillance, they found it easier as it was possible to actually have more opinions.

"It is difficult being an enforcement organization due to the situation in-between different interest groups. Auditors are on one side and the authorities on the other. It is difficult to achieve some kind of balance. The second difficulty is the subjectivity of IFRS; partly through the design and the rules of importance. There is a clear difference between the interpretations of authorities and companies. Furthermore, the size of IFRS, makes it almost unreadable. One cannot take in that amount of information."

During the interviews, the enforcement bodies reasoned around the fact that it is not difficult to identify the errors just because it is principle based, however to sanction a principle based system is more complicated. No matter how well or clearly formulated a principle or rule is; there will always be different interpretations made. Due to this, we find the role of IFRIC to become more and more important. If their work is not done well and as fast as the demand for interpretations call for, the risk of having the enforcement bodies issuing suggestions on how to interpret the principles is significant. This might also be a risk as the reader of financial information has to take. FEE (2002:41) and Brown and Tarca (2005:182) are arguing that one single European enforcement body is not possible at the moment due to different legal jurisdiction, but it is preferable. From this perspective, we find the likelihood of in the end moving towards a Swedish GAAP rather than an IFRS GAAP, if the situation continues as today.

5.1.4 Can There Be a Speed of Action From FI and OMX?

It is vital according to the FEE suggestions on good enforcement number five (Confidentiality and speed of action) that the market is receiving information about noncompliance as fast as possible. This is not an issue according to FI and OMX and the rest of the respondents. The market normally gets the information through other media if something is material⁵ with the financial information. The auditor plays a vital part and should inform the market if something is material according to our respondents. Concerning the work done by OMX, they argue that the speed of action is impossible from the beginning.

"We are looking at old information from the start when receiving the companies' reports. The only time you can actually correct information is when it is created. We

⁵ "The information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statement" according to IASB Framework paragraph 30.

are looking at defects on a more principal level and this is information that often doesn't affect an investor's decision."

Again, as mention before, what difference does the enforcement from FI and OMX make if they only can correct old information? There seems to be consensus from the respondents that enforcement bodies can play an important role in making the financial information transparent and better for the investors. But when considering that they more or less only can find a lack of disclosure and they only are correcting financial information that is already old; one can ask what difference does the enforcement make and how much do they contribute to make the financial information better and more trustworthy? Since enforcement of IFRS today is based upon already published information in the financial statements, we find speed of action to be significant in order to achieve a relevant outcome today. The corrections and non compliances must be resolved quickly.

5.1.5 The Possibilities for OMX to Find Something Material

When considering the possibility for the enforcement bodies to discover something that is material⁶, all but one of the respondents finds it unlikely and difficult. The respondents say that if someone should discover anything, it should be attesters (the auditors). One of the attesters said about the work of OMX:

"They sit and read annual reports, they would do more good through investigations on the spot, but they don't. Through these they would be able to discover a lot more. However, from the annual reports they are able to get an indication. To conclude, they are able to do more efficient work but omit to do it. They seem pleased after their desk-top reviews."

We discussed in chapter one *Background* about what purpose the enforcement bodies really can fill. When asking the attesters and the preparers, seven out of nine perceived that they filled a purpose with adding more credibility to the financial information. On the other hand, according to OMX their ability to find something that hasn't been discovered by an auditor is very small.

"As you understand, our possibilities to find something are not good. What we can find is if the company hasn't made proper disclosures. In order to find mistakes about how they have valued something you have to look deeper into the accounting."

When OMX discover something that is perceived as non-compliance with IFRS they send a letter to the company and start a dialogue about the specific issue. According to FEE suggestions on good enforcement number one (Support for high quality corporate governance and external audit) an effective enforcement relies upon all those with influence on financial reporting playing their part. It is vital that enforcement bodies have contact with and discuss IFRS issues with the auditors as well. Norberg and Thorell (2009:125) mention the same consideration when they say that enforcement and auditing seems to be two parallel but separate functions with an unclear inter relation. We believe that role of the enforcement and the enforcement bodies' work can be more efficient if they are open for dialogue with each other. It is important not to forget as the "EU Financial Reporting Strategy: the way forward" mention; enforcement appears in is approximately six levels. The first enforcement mechanism starts with self-enforcement when the management are the responsible body for the creation of the financial statement. A dialogue with them and with the auditors could make the financial information better.

⁶ "The information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statement", IASB Framework paragraph 30.

5.1.6 The Lack of Resources

According to CESR's "Standard No.1 on Financial Information – Enforcement of Standards on Financial Information in Europe" (see Appendix 4) the enforcement bodies should have the necessary powers and sufficient resources to function as an actual enforcement body. OMX have complained about their lack of resources to achieve a sufficient enforcement in the "Framställan om ändring av lagen (2007) om värdepappersmarknaden avseende redovisningstillsyn" where they not wish to continue with the enforcement obligation. They are addressing different bottle necks, such as:

1. The negatives with not having the right competence in house,
2. To do surveillance on their customers, as a profit driven company, and
3. That OMX is not the only body taking care of enforcement, as NGM is involved as well.

By looking at Nobes and Parker's (2006:175) way of dividing different enforcement into categories, Sweden is placed under stock exchanges together with Norway and Switzerland (see 3.4 *Different Enforcement Bodies in Europe*). One can ask if the surveillance in Sweden really should to be in this category. Not that Nobes and Parker are placing them under incorrect category, more if it is suitable from a trustworthiness aspect towards the financial information. Our skepticism becomes stronger when the attesters and the preparers were questioning OMX's competence and their ability to function as an enforcement body. Whether this questioning of competence comes from rumor or actual fact is difficult to prove but the attesters and the preparers that have been in contact with OMX had the same opinion.

"Sometimes it feels we know more than they OMX do. They were feeling obligated to respond to our request and gave us an answer that felt simple. It felt that we were not on the same level."

It is difficult to understand how FI can delegate the task of enforcement to a body that apparently does not want to have it. We agree with the attesters and the preparer and find it strange that a profit driven company as OMX does the surveillance. As mentioned before, FI is the only representative body from Sweden at CESR's annual meeting and OMX perceive this as a disadvantage. That OMX is outside this cooperation is aggravating and makes the exchange of information not as efficient as it could be according to our interview person at OMX. OMX seems also not to have the sufficient resources or the will to put more resources into the project. Despite the LVPM law that OMX has to follow, the incentives for doing a job beyond what the law is requiring is not likely with the information we have gathered during our interviews.

5.1.7 The Misallocation Between Reviewed Financial Information and Other Information

One interesting issue mentioned by the respondent from OMX is what kind of information they should focus when doing their surveillance.

"Today there is a misallocation between reviewed information and other. A lot of resources are put towards information already reviewed by auditors."

As Norberg and Thorell (2009-116-7) mention, there is a clear lack of guidance on how the surveillance should be done. Apart from what is said in the LVMP law, OMX is using a risk based approach when reviewing the financial reports. Maybe a better guidance on what to review from FI would avoid the situation as the respondent from OMX is mentioning? Or maybe it is

beneficial that OMX is reviewing the same material as the auditors do? If they would not, the risk is that auditors would feel less pressure that their work is reviewed one more time.

Another aspect worth mentioning is FEE's feature for an effective enforcement number seven (Focusing resources). This enforcement suggestion proposes that an enforcement body should avoid time consuming and expensive investigations of relatively minor matters of non compliance. This implication support the one mentioned by the respondent from OMX when he talked about the misallocation of reviewed information. The resources used from OMX would do better if they could investigate information of more material kind instead of spending time on disclosure issues he continued.

5.1.8 Summary of Research Question One

With help from our interieus and our frame of reference, we have in this part of the chapter concluded that the amount of information to the public from FI and OMX about their enforcement obligation is seen as insufficient. The attesters and preparers are demanding more information about activities concerning enforcement. There seems to be, as some respondents put it, a black hole after Panelen left the scene.

IFRS are further moving more towards what US GAAP is today according to our respondent from OMX. The challenges with enforcing a principle based standard might be the answer why there is such development he continues. The challenges with enforcing the standard have also led to the question if OMX should act as a normative body and not only have a surveillance role.

Almost a unison voice from prepares and attesters said that FI and OMX can do much more to improve the surveillance. Today, the only thing that OMX are able to find with their amount of resources is a lack of disclosure and one can argue what this actions add to create a better trust for the financial information? The respondent from OMX said himself that there was a misallocation of what kind of information they should take a deeper look at.

5.2 Research Question Two

Is there a trust from the preparers and attesters for the work with enforcement of IFRS today done by FI and OMX and if so, how is it expressed?

5.2.1 The Perception of Trust in Relation to the Financial Statements

The perception of trust among the respondents were somewhat similar and can be summarized into three concepts; clearness, consequence, and mutual understanding. The agreeableness between the respondents is an uplifting result, as trust is perceived to be a necessity today (O'Hara, 2004; Clarke, 1999). One of the respondents elaborates further and says:

"It is crucial that parts that are involved in the financial process can be trusted and are as transparent as possible. Just the rumor that someone is acting in an incorrect way can damage the trust and soundness of the financial reports"

With this statement in mind, the trust towards the work that FI and OMX becomes important and shows that it is a pressing issue to discuss. During the interviews we found trust to be the foundation to everything, according to almost all respondents, which also illustrates and pinpoints the accuracy of studying the surveillance of financial statements in relation to the concept of trust. This result is also what we perceived it to be. Therefore, the notion of whether the work by FI and OMX increase the trust towards the financial statements is an urgent topic. The attesters and preparers somewhat agree to that the opinion from the enforcement bodies increase the trust of the financial statements. However, the possibility and ability of it to grow even stronger is emphasized. Despite this, one of the preparers differs significantly in the perception regarding whether there is an increase in trust or not.

"No, I believe there is not. The relation between FI and Börsen is unclear, and the mandate from FI is vague. However, of course there should be a surveillance but with clear missions"

This statement suggests that due to unclear insight into what the enforcement bodies are doing, also discussed earlier in this chapter, the total increase in trust is uncertain. However, to clarify, all the attesters agree that there is an increase of trust to the financial statements through the opinion from enforcement bodies, although it is only a piece among others in a puzzle, as one of the attesters chose to explain it. We wonder, how much more can the trust towards the financial statements increase through their opinions? This since the findings point towards it not being as efficient today as it could be.

The enforcement bodies themselves are uncertain to whether their work today really contributes to an increased confidence towards the financial statements. However, they agree that it should be the case. OMX further defined how in this case it could contribute to an increase in trust, and explains that it is the actual knowledge of someone investigating and reviewing the financial reports, which strengthens the credibility. This corresponds to what Clarke (1999:25,146) said about trust; there is no need for the whole truth when we trust. This author also mentioned that trust between actors may allow for a reduced uncertainty and generalised expectations of behaviours. According to us, the knowledge of the enforcement bodies reviewing the financial statements may be enough to generalise their work to involve more thorough procedures than what is actually the case. As the companies are aware of this review they are probably more unwilling to differentiate too much, and become too creative with their accounting. So, with the reasoning made by OMX in mind, it may be possible to claim that although the enforcement

bodies' opinion today may not contribute to an actual creation of trust, the fact of having someone reviewing the statements may be enough to increase the trust. We wonder if one should believe the attesters and preparers in their perception of whether there is an increase in trust or not, as this is not trustworthy. This since the enforcement bodies performing the enforcement say it is hard to tell. Is it really an increase in trust? Maybe there is an increase in trust by just having surveillance, as OMX reasoned, but the actual work done does not make a difference on the financial statements at all. Is this reasoning and perception really applicable in the long-run?

5.2.2 Labelling and Identifying the View of Trust Today

We will continue to discuss trust towards the enforcement bodies in relation the perception of their competence and their responsibility by discussing what Das & Teng (2001:255-7) stated. There are two dimensions of trust; competence trust and goodwill trust. The former involves the expertise, ability and technical competence. One of the interview questions relate to competence trust, as we asked if there was a trust for the competence of FI and OMX. One of the attesters said:

"I trust their ambitions. I do not trust their overall competence; however, this is related to the lack of transparency. The level of education is irregular sometimes between us and Börsen. More specifically about the competence at Börsen is that it has been a bit floppy between Börsen and FI, and the cases between company X and Börsen have not involved a sufficient level competence according to us. "

Although this is a quotation from a specific respondent, almost all of the attesters and prepares are questioning their competence. Through this, we find that here is a lack of competence trust towards the enforcement bodies in Sweden today, when considering the technical competence. As they seem to not possess adequate expertise within this field. We find this intimidating; how can there be an actual creation of trust towards the financial statements if the enforcement bodies do not have satisfying competence to perform their investigations? This is interesting because when we relate this to the previous discussion, the outcome here contradict. Is the trust that the attesters and preparers experiencing towards the financial statements a false trust?

Furthermore, as FEE's second suggestion (High quality, expert, globally-consistent decisions on important issues) for an efficient enforcement states, IFRS needs to be applied rigorously and consistently with high-quality and experts on important issues. However, are the enforcement bodies in Sweden experts in this field? Are there other organizations more suited for enforcement issues?

Eight of the ten preparers and attesters perceived that OMX were lacking competence in some way or another. OMX are, according to some respondents, understaffed and could make a much better work if they were more people in place. The criticism is as well on individual level; one respondent was skeptical last time he was in contact with OMX and their response to an addressed question:

"It didn't feel as we were on the same level. It felt like we knew a lot more about the subject than OMX. I understand that they can't know everything of course but the level on the answer we got back was not what we expected"

In relation to number five of FEE's features for an efficient enforcement (Confidentiality and speed of action), the aspect of competence trust towards the enforcement bodies is important. Errors and mistakes may lead to the creation of false market, both considering shares and debt instruments. If the enforcement bodies do not have sufficient competence, the issues related to noncompliance will not be resolved quickly, which in turn involves wrong information to market

participants. One of the respondents elaborated further and said that OMX still seems to be handling incidents and errors that happened a long time ago, and are not reacting upon issues and noncompliance taking place today, to the same extent. We find this not to contribute to a creation of trust towards the financial statements nor the enforcement bodies. However, this is probably not only a result of a lack of technical expertise. One should not underestimate the fact of not-yet-established routines and procedures, since this may also be a possible answer and explain why they are falling behind in the cases and investigations.

To relate the aspect of trust to the second dimension discussed by Das & Teng (2001:255-7), goodwill trust involves the responsibility, intentions, integrity and moral obligations. We wonder if OMX really is the most appropriate organization for the job. Further, an insufficient goodwill trust could make controlees, in this case the attesters and the preparers, to question if the controllers (the enforcement bodies) pursue private interests instead of the mutual understandings. Through this, we emphasize again that OMX is a private company with a clear interest for profits. Is this really a moral obligation and does it live up to the expectations of integrity? As OMX both is an issuer of trading lots, and through this making profits out of the listed companies, how can they act as an impartial investigator when reviewing annual reports? According to us, there is an obvious conflict of interest and the appearance of goodwill trust should be questioned. FEE also warn about this in their features for effective enforcement number three (Freedom from bias), and says that the enforcement body shall take every safety precaution that is necessary to avoid a biased decision. As mentioned before, OMX is a profit driven company, and we wonder how much this can affect the decision made about certain decisions. Or put it this way, we don't believe that such a large and professional organization as OMX would make any unbiased decision on purpose. But, as also mentioned before, FI is not compensating OMX for their surveillance and the reluctant to make more investigation than is necessary can contribute to biased decision, or maybe, decisions that are more or less unsupported.

As Rothstein (2003:21-2) discussed, an efficient cooperation is created through the work towards common means, which only can arise through trust. However, if one cannot trust that the other partners will cooperate, it becomes pointless to decide for oneself to. As discussed in this section, it is unclear whether the enforcement bodies create competence trust and goodwill trust today, according to the attesters and the preparers. This may create a social pitfall where it becomes pointless for the creators to cooperate with the enforcement bodies as they may not perceive a trust towards their work. Rothstein (2003:30) also mentioned that the theory of social pitfall is important to consider due to that once in the problem of a social pitfall it is hard to break away. Trust is a highly psychological phenomenon and no matter how rational it may be, it is hard to forget something. We find it urgent for the enforcement bodies to take these perceptions from the preparers and the attesters into account; which is highly related to the work of transparency and expertise.

5.2.3 Creation of Trust

Considering a possible building of trust, Rothstein (2003:173) discuss whether the work of a public sector can contribute to the creation of trust.

*“Trust, both considering toward individuals and institutions, is hard to earn but easy to destroy”
(Rothstein, 2003:199).*

According to Rothstein (2003:263-5), Sweden is a typical example of where trust towards the political institutions and the public sector is low. Especially when considering trust towards the

government, the Parliament and the parliamentary parties. We would like to relate this to the actual starting-point for FI as a parliamentary organization. As the trust towards these kinds of organizations, in general, is relatively low we find it necessary to stress the fact of performing an efficient enforcement and that they have the necessary competence. This to create trust, and as Rothstein (2003) stated, trust is hard to earn and easy to destroy.

It should be in the interest of the enforcement bodies to increase trust. As both FI and OMX are unsure whether their work actually increases the trust towards the financial statements one can wonder if the work is actually focused upon increasing the quality of the financial statements or if it is only about getting the surveillance done. Are they performing their best considering the situation and this being a new task for them to undertake? We find it important to emphasize the perception of FI among the attesters and preparers could partially be related to that FI is a parliamentary organization and may start off with a weak position only due to that. An insight into this kind of hurdle is important to be aware of as it may affect the fundamental view of FI and their involvement in the enforcement of IFRS today which may in the end affect the possible creation of trust.

Another interesting aspect of trust to discuss is the one related to control. As Das & Teng (2001:263-5) argue, control should not only be associated to its harm of trust because regulation may create a sense of mistrust, control may also increase trust as people can justify their actions. This comes from the knowledge about whether they do their jobs well or not. However, we find it not to be a situation creating trust. This since hardly any of the respondents actually notice and hear anything about the work of the enforcement bodies. How is it then possible to use this as a notion about whether one is performing a job correctly or not? This is another indication of distrust towards the work by FI and OMX.

According to investigation made by the Swedish government (SOU 2004:153), one can apply a triangular approach to the creation of trust. This approach takes the aspect of regulation in relation to trust one step further than what Das and Teng (2001) discussed.

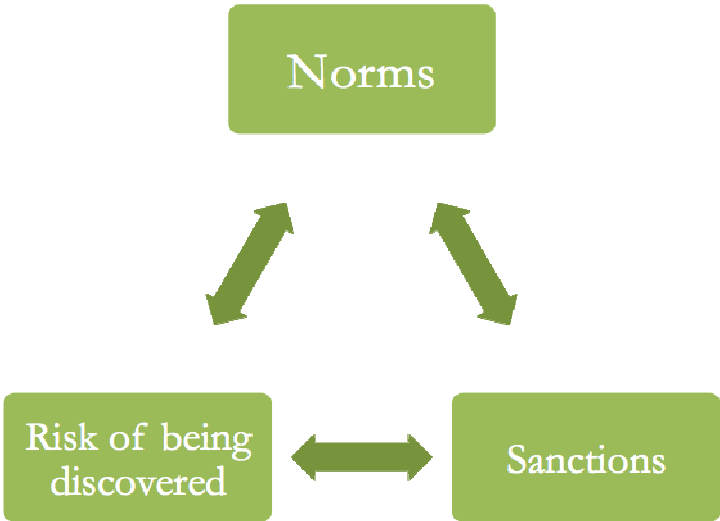


Figure 6 Triangular Approach to the Creation of Trust (SOU, 2004:153)

It is not enough with regulation in order to create trust towards the financial statements. There also has to be a risk of being caught and sanctions. (SOU, 2004:153). With this in mind, although the norms and regulations are well formulated, which is possible to consider CESR and equivalent Swedish version is, trust is not created without sufficient risks of being caught and a

severe sanctioning system. We find this to somewhat conclude the discussions made earlier in this chapter. As we have questioned if the surveillance today contribute to a creation of trust. According to this model (see Figure 6 *Triangular Approach to the Creation of Trust* above) trust is only created when all three aspects in the triangle are in balance.

When considering sanctioning and the risk of being discovered, one can relate to FEE's suggestion number nine (Sanctions) in order to ensure decisions and rectifications are implemented. The interview questions related to sanctions also incorporated the possible difficulties of sanctioning a system that is principle based and through this includes a lot of subjectivity and balancing between different aspects to consider. The enforcement bodies both reasoned around the fact that it is not harder to identify errors just because the system is principle based, however the sanctioning is complicated due to the different interpretations and exceptions. OMX said:

"The problems with a principle based system are the estimation part in the financial reports. This is where the companies themselves decide the valuations. All entries that are of significance almost always originate from estimations and affect the financial information. It is hard to question these. One can discuss these with the companies but in the end it is hard to tell whether it is right or wrong. What is interesting here is the surveillance, where it is about judgments and the analytical skills. There are large scales of freedom in the system today and these types of questions put pressure on companies. One should not think that just because no errors are found everything is correct."

One can wonder how effective the sanctioning in Sweden actually is, when considering the enforcement bodies' perceptions about it and the difficulties involved. We still though want to clarify that the sanctions possibilities that FI and OMX possess is in line with both FEE's features for effective enforcement number eight (Rectification of defective financial information) and CESR's "Standard No.1 on Financial Information – Enforcement of Standards on Financial Information in Europe" (see appendix 4). FEE's features number eight states that the enforcement body should have proper rectification and should be able to start a court case. CESR's mentioned the same issue as FEE. We are confident that FI and OMX would take all actions necessary if a company would violate IFRS standard but, again, in order to take necessary actions, you have to be able to find them. Due to the questioned competence, discussed earlier in this section, the sanctioning in Sweden might be possible to become more effective. The preparers somewhat agreed that a principle based system enables more individual judgment, and through this, it is harder to sanction, this also seems to be preferred. The attesters also said during the interviews that a system like this is hard to sanction. The preparers' and attesters' perceptions imply that it is hard to get sanctioned as the principle based system calls for interpretations and balancing in specific cases. Due to the aspect of sanctions, this part of the triangle does not measure up with the other two. And, as mentioned earlier, if the three parts in the triangulation are not in balance, it is difficult to create trust.

As discussed earlier in this chapter, the likelihood for OMX to discover anything material that has not been discovered by the auditor is low. Relate to the previous accounting scandals, e.g. Enron, the auditors have more or less been involved in the fraud and creative accounting decisions made. If there is no likelihood that OMX will discover anything material, it is not possible for us to indicate anything else than that the triangle of trust is not in balance. As the risk of being discovered is low, the possibilities of being sanctioned can be questioned and it is not possible to find a balance with the norms and regulation occurring today.

5.2.4 Summary of Research Question Two

With help from our intercieus and our frame of reference, we have in this part of the chapter concluded that trust is the foundation to everything, according to almost all of the respondents. The attesters and the preparers agree that surveillance today contributes to a creation of trust; however, due to an unclear insight into what the enforcement bodies are doing, the total increase in trust is uncertain. To clarify, all the attesters agree that there is an increase of trust to the financial statements through the opinion; however it is only a piece among others in a puzzle, as one of them chose to explain it.

There seems to be general lack of trust among the attesters and preparers when considering the enforcement bodies' technical competence. Through this, we question how strong the trust mentioned above actually is.

When considering the creation of trust, illustrated in Figure 6 Triangular Approach to the Creation of Trust, we conclude the three concepts are imbalanced. The concept of norms and regulation as well as the possibilities to sanction are well formulated and achieved. The creation of trust is difficult but when considering the risk of being discovered, the possibilities for OMX to find something material is small.

6.

Conclusion

Trust, as we have learned through this thesis, is a fundamental and crucial aspect for parts involved when creating financial information. We want to conclude our discussion from the last chapter in this conclusion and, as stated in the purpose, make suggestions on how FI and OMX can build a better enforcement system with trust as the foundation.

6.1 Answering our Purpose

The purpose of this thesis was to find an answer to:

- Has the trust changed for the Swedish financial reports based on IFRS with the enforcement work done by FI and OMX, and if so, why?

This thesis has found evidence suggesting that trust towards the financial statements has changed, unfortunately to the worse. Although there is a perception today among the preparers and the attesters that the work contributes to a creation of trust, the magnitude and actual impact are hard to specify. Due to the transparency, competence and impact of the surveillance made by Panelen previously, there is not an increased trust towards the financial statements in comparison to the situation today.

Why? To begin with, we emphasize the issue of transparency. The general knowledge about the enforcement today, responsible organizations and situations when either FI or OMX have sanctioned a company for not following IFRS' rules, were low. FI and OMX agreed and were aware of to the lack of information flow and the shortage of information at the homepages. However, FI referred to it as partially a cause of a disinterest towards the work with surveillance today. To clarify, we have not noticed any indication among the attesters and preparers that there is a disinterest towards the work done by FI and OMX.

Secondly, there is a general perception among the attesters and preparers that the enforcement bodies in Sweden do not possess adequate technical knowledge and expertise. It is difficult to increase the trust towards the financial statements if the organizations handling the surveillance do not have the necessary capabilities for the job. In comparison to the opinion about the competence and expertise within Panelen, the competence trust towards FI and OMX today is significantly lower.

Thirdly, it can be concluded that the notion of someone reviewing the financial statements seems to make the attesters and preparers perceive an increase in trust towards the financial statements. However, this does not matter if the possibilities to discover anything considered to be material and accurately are low. OMX clarified the misallocation of reviewed information and what kind of information that is worth focusing upon and mentioned that the resources would do better if they reviewed information of more material kind instead of spending time on disclosure issues.

Thus, the trust towards the financial statements would increase if the enforcement bodies were able to review the same material as the attesters do.

We, including some of the respondents, find it difficult to understand why OMX, as a profit driven company is handling the enforcement in Sweden. Through this, we wonder if the responsible organization for the actual surveillance and enforcement in Sweden instead should be FI alone, not OMX and NGM. Since OMX has given a written reluctance saying that they don't want to have the responsibility anymore (see section 3.2.2 *Nasdaq OMX Stockholm (OMX)*). With more than one company responsible for surveillance, the standardization of enforcement can be scattered. Since FI is a member of the CESR committee, we find them to be more appropriate for developing the routines concerning the surveillance and are more updated.

6.2 Suggestions on How to Build an Increased Trust to the Financial Information

As part of the purpose, we have made suggestions to FI and OMX on how they can improve their trust towards themselves as organizations and build stronger trust to the financial information. First of all, in order to create trust we suggest the enforcement bodies actually reveal their working procedures to make it more transparent. As we discussed under research question number one, we found it highly time consuming to grasp the relation between FI and OMX, and the perception among the attesters and preparers seem to fall in line with ours. Trust towards the financial statements is not created through a general lack of knowledge, there has to be transparency to the procedures and the work done by the enforcement bodies today.

- Better informative information online and more explanations about their working procedures.

Moreover, we find it necessary for FI and OMX to create sufficient competence trust. In order to achieve this, they need to recruit employees representing both attesters and preparers, as well as people with expertise within accounting and enforcement, this to really understand the considerations made by both preparers and attesters today.

- More specialised staff with knowledge about IFRS

As OMX said, "There is a misallocation between reviewed information and other", and too many resources are allocated towards reviewing information that is already thoroughly reviewed by auditors. We agree with OMX that it would be more logical for OMX to investigate issues that more potentially could be material. This is what we believe they would be best at performing. In order to actually find something, not found by auditors, they have to be closer to the companies and almost stand by their side during the discussions about different deliberations and considerations. We believe it is a good suggestion that OMX should act as a watchdog for the surveillance agent. And based upon their reports choose to more thoroughly investigate those companies who are most likely to have errors.

- Work more closely with attesters (the auditors) and preparers (the companies)

6.3 Further Studies

As we chose not to include the investors in this thesis, a study investigating their interpretation of whether the trust towards the financial standards has changed, and if so why, would be interesting to investigate. Furthermore, we believe our findings in relation to this would combined be very interesting, especially for the enforcement bodies today.

Furthermore, it would be interesting to study the perceptions of enforcement in other European countries. To start with, is it different from Sweden? Do they find that the trust towards the financial statements has changed? All other countries are probably not using a private organization such as OMX to perform their job. How do they perceive the situation today?

Another suggestion is investigate the work made by SEC in USA. Perhaps the enforcement procedures differ significantly from those issued by CESR. Moreover, as there is a rule based system present in USA, how is the sanctioning executed there?

7.

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Appendix 1

Interview questions to preparers (the companies) and attesters (the auditors)

Introduction

- What is your position and what have you done before?

The work done by enforcement bodies (FI and OMX)

- Tell us how the relation is between FI and OMX and who has the responsibility for the enforcement for IFRS.
- From November 1st 2007, the new law (LVMP) came. Has the law meant any changes for you company?
- Was there a need of change?
- What is the purpose of the surveillance/enforcement made by OMX?
- Do you remember a situation when either FI or OMX has sanctioned a company for not following IFRS rules?
- When shall FI and OMX take actions?
- Shall OMX act as a normative body and not just as an enforcer of IFRS?
- What is a violation of IFRS standard according to you?
- Exemplify a clear and a non-clear violation of IFRS standard.
- What is your opinion about OMX ability to find something that is material and violating IFRS standards that hasn't been discovered by an auditor?
- What kind of materiality can OMX possibly find?
- IFRS is perceived to be a principle-based standard (contrast to US GAAP) where the interpreter can use its individual judgment to interpret the standards. Do you see any issues with sanctioning such system?

Trust towards the enforcement bodies (FI and OMX)

- Trust is one of the keystones for producing sound financial information. What does trust mean to you?
- Is there a need for further investigations of the auditors work concerning the financial information?
- Do you consider that FI and OMX is creating trust to the financial information?
- Do you have trust for FI and OMX's competence?

Appendix 2

Interview questions to the enforcement body Finansinspektionen (FI)

Introduction

- What is your position and what have you done before?

The work done by the enforcement bodies (FI and OMX)

- How is the communication between FI and OMX?
- What is the purpose of the surveillance/enforcement made by OMX?
- Was there a need to change from how it was before?
- IFRS is perceived to be a principle-based standard (contrast to US GAAP) where the interpreter can use its individual judgment to interpret the standards. Do you see any issues with sanctioning such system?
- What is your opinion about OMX ability to find something that is material and violating IFRS standards that hasn't been discovered by an auditor?
- How do you and OMX handle the communication to the market and the auditors?
- How do you at FI inform the market about FI's activities?
- How fast are you at FI to correct errors in the financial information?
- Shall OMX act as a normative body and not just as an enforcer of IFRS?
- What are FI possibilities to prosecute a company for not following IFRS rules?
- What is a violation of IFRS standard according to you?

- Exemplify a clear and a non-clear violation of IFRS standard.
- What kind of materiality can OMX possibly find?

Trust towards the enforcement bodies (FI and OMX)

- Trust is one of the keystones for producing sound financial information. What does trust mean to you?
- Do you consider that OMX and the work done by FI create a larger trust towards the financial information?
- How has trust change since Övervakningspanelen disappeared?
- How is the trust for OMX if we ask the same question to the market?
- In the publication "Framställan om ändring av lagen (2007:528) om värdepappersmarknaden avseende redovisningstillsyn" OMX no longer want to the surveillance/enforcement role. What do you consider about that?
- Do FI have the necessary competence for an efficient enforcement?
- What is the most difficult thing when working with enforcement?
- If you had the power to change anything in the enforcement system today, what would that be

Appendix 3

Interview questions to the enforcement body Nasdaq OMX Stockholm AB (OMX)

Introduction

- What is your position and what have you done before?

The work done by the enforcement bodies (FI and OMX)

- How is the communication between OMX and FI?
- What is the purpose of the surveillance/enforcement made by you at OMX?
- Was there a need to change from how it was before?
- IFRS is perceived to be a principle-based standard (contrast to US GAAP) where the interpreter can use its individual judgment to interpret the standards. Do you see any issues with sanctioning such system?
- What is your opinion about OMX's ability to find something that is material and violating IFRS standards that hasn't been discovered by an auditor?
- How do you at OMX and FI handle the communication to the market and the auditors?
- How do you at OMX inform the market about OMX's activities?
- How fast are you at OMX to correct errors in the financial information?
- Shall you at OMX act as a normative body and not just as an enforcer of IFRS?
- What are FI possibilities to prosecute a company for not following IFRS rules?
- What is a violation of IFRS standard according to you?

- Exemplify a clear and a non-clear violation of IFRS standard.
- What kind of materiality can you at OMX possibly find?

Trust towards the enforcement bodies (FI and OMX)

- Trust is one of the keystones for producing sound financial information. What does trust mean to you?
- Do you consider that OMX's work and the work done by FI create a larger trust towards the financial information?
- How has trust change since Övervakningspanelen disappeared?
- How is the trust for OMX if we ask the same question to the market?
- In the publication "Framställan om ändring av lagen (2007:528) om värdepappersmarknaden avseende redovisningstillsyn" OMX's no longer want to the surveillance/enforcement role. What do you consider about that?
- Do OMX have the necessary competence for an efficient enforcement?
- What is the most difficult thing when working with enforcement?
- If you had the power to change anything in the enforcement system today, what would that be

Appendix 4



STANDARD NO. 1 ON FINANCIAL INFORMATION

ENFORCEMENT OF STANDARDS ON FINANCIAL INFORMATION IN EUROPÉ

Foreword

This first standard on Enforcement of Standards on Financial Information in Europe has been developed by CESRfin through its Sub-Committee on Enforcement (SCE). The standard is a principle based standard.

CESRfin's Work Plan, which was approved by CESR in January 2002, includes the development of principles, guidelines and standards in the areas of:

- definition of enforcement;
- selection techniques;
- powers to be attributed to the enforcers;
- cross border listings and offerings.

The first two areas are described in the principles of this standard but may need to be expanded on in a later standard.

As regards the other two areas the SCE will develop a new work plan which will be aimed at providing for a sufficiently complete set of standards by 2005.

The SCE is currently working to develop principles on powers to be attributed to enforcers which will be finalised in the short term. Thereafter the SCE will develop enforcement principles related to cross border listings and offerings.

As regards the coordination between CESR and non-CESR members in the area of enforcement CESRfin will establish an appropriate mechanism whereby CESR members and non-CESR members may discuss enforcement issues in order to achieve a high level of coordination and convergence in the enforcement decisions.

A CONTEXT AND SCOPE OF THE STANDARD

On the 13th of June 2000 the EU Commission issued a Communication¹ to the Council and the European Parliament on the future EU financial reporting strategy. The new approach, which has been implemented by a EU regulation² adopted by the EU Council on 6 June 2002, is based on the introduction of the International Financial Reporting Standards (IFRSs) or International Accounting Standards (IASs) ³ in Europe.

Further steps toward harmonization in the EU have also been taken in the field of disclosure including directives on prospectuses and periodic reporting.

B DEFINITION OF ENFORCEMENT

Principle 1

The purpose of enforcement of standards on financial information provided by the issuers mentioned by principle 9 is to protect investors and promote market confidence by contributing to the transparency of financial information relevant to the investors' decision making process. With regard to financial statements, the above implies that enforcement contributes to a consistent application of the IFRSs in the EU financial regulated markets.

Principle 2

For the purpose of this standard enforcement may be defined as:

- monitoring compliance of the financial information with the applicable reporting framework;
- taking appropriate measures in case of infringements discovered in the course of enforcement.

The reporting framework includes the accounting and disclosure standards adopted by the EU.

C ENFORCERS

Principle 3

Competent independent administrative authorities set up by member States should have the ultimate responsibility for enforcement of compliance of the financial information provided by the issuers identified by Principle 9 with the reporting framework.

Principle 4

Other bodies might carry out enforcement on behalf of the competent administrative authorities, provided that these bodies are supervised by and responsible to the relevant competent administrative authority.

Principle 5

Irrespective of who carries out enforcement any standard on enforcement established by CESR should be complied with.

Principle 6

Competent administrative authorities shall have adequate independence from government, and market participants, possessing the necessary powers and having sufficient resources.

Principle 7

The necessary powers – which may be delegated to those acting on behalf of the competent independent administrative authority – should at least include power to monitor financial information, require supplementary information from issuers and auditors, and take measures consistent with the purposes of enforcement.

Principle 8

The competent administrative authorities should be responsible for:

- the setting up of an appropriate due process of enforcement consistent with the application of the principles hereby stated;
- the implementation of that due process.

D ISSUERS AND DOCUMENTS

Principle 9

The principles for enforcement here identified should apply to financial information provided by issuers:

- a) whose securities are admitted to trading on a regulated market;
- b) that applied for admission to trading of their securities on a regulated market.

Principle 10

The principles for enforcement here identified should apply to financial information provided by all harmonized documents, including annual and interim financial statements and reports, prepared on individual and consolidated basis as well as prospectuses and equivalent documents.

E METHODS OF ENFORCEMENT

Principle 11

For financial information other than prospectuses ex-post enforcement is the normal procedure, even if pre-clearance is not precluded.

Principle 12

For prospectuses ex-ante approval is the normal procedure as specified by the EU directives, which also identify the nature of the approval. Ex-post enforcement of financial information provided by prospectuses is possible as a supplementary measure.

Principle 13

Enforcement of all financial information is normally based on selection of issuers and documents to be examined. The preferred models for selecting financial information for enforcement purposes are mixed models whereby a risk based approach is combined with a rotation and/or a sampling approach. However, an approach based solely on risk may be an acceptable selection method. A pure rotation approach as well as a pure reactive approach is not acceptable. However, indications of misstatements provided by auditors or other regulatory bodies as well as well grounded complaints should be considered for enforcement investigations.

Principle 14

In order to allow enforcers to adopt gradually the selection methods provided for by Principle 13, a mixed selection technique based on a combination of a random selection and rotation is considered a workable transitional step. However, such a methodology should be designed to give an adequate level of detection risk.

Principle 15

Methods of enforcement on selected information cover a wide spectrum of possible checking procedures, ranging from pure formal checks to in-depth substantive in-nature checking. The level of risk should normally determine the intensity of the review to be performed by the enforcers. The type of document to be examined and the level of information available on the issuer is also to be taken into consideration.

F ACTIONS

Principle 16

Where a material misstatement in the financial information is detected enforcers should take appropriate actions to achieve an appropriate disclosure and where relevant, public correction of misstatement (in line with the requirements of the reporting framework). Non-material departures from the reporting framework will not normally trigger public correction even though they normally deserve an action as well. Materiality should be assessed according to the relevant reporting framework.

Principle 17

Actions taken by the enforcers should be distinguished from sanctions imposed by the national legislation. Actions are measures generally aimed at improving market integrity and confidence.

Principle 18

Actions should be effective, timely enacted and proportional to the impact of the detected infringement.

Principle 19

A consistent policy of actions should be developed, whereby similar actions are adopted where similar infringements are detected.

G COORDINATION IN ENFORCEMENT

Principle 20

In order to promote harmonization of enforcement practices and to ensure a consistent approach of the enforcers to the application of the IFRSs, coordination on ex-ante and ex-post decisions taken by the authorities and /or delegated entities will take place. Material controversial accounting issues will be conveyed to the bodies responsible for standard setting or interpretation. No general application guidance on IFRSs will be issued by the enforcers.

H REPORTING

Principle 21

Enforcers should periodically report to the public on their activities providing at least information on the enforcement policies adopted and decisions taken in individual cases including accounting and disclosure matters.