Activity Report 2010

Supervision of Financial Reporting

January 2011

Contents

1 Summary

This activity report is published by the Netherlands Authority for the Financial Markets [*Autoriteit Financiële Markten*, or AFM] to inform the public regarding its activities in relation to its supervision of financial reporting in the 2010 calendar year. This year, only brief attention will be devoted to the findings as a result of supervision, since most of these have already been published on 2 November 2010 in ‘Items of Attention in Financial Reporting for 2010’[1]. As a result of this earlier than usual publication, the AFM expects the identified areas of improvement to be addressed in the financial reporting for 2010.

In response to suggestions from the market, the AFM is taking a less formal approach in certain areas. This is shown for instance by the language and tone of requests for further information, in the way the situation is addressed, and the issuance of requests for further information [*verzoeken om nadere toelichting*] and notifications [*mededelingen*] in the

[1] *http://www.afm.nl/layouts/afm/default.aspx~/media/files/fin-verslag/items-attention-fv-2010-eng.ashx*

follow-up review[2] only in the second instance. Furthermore, some of the investigations still outstanding from 2009 were not formally concluded with a notification, instead agreements were made regarding the inclusion of the AFM's findings in the 2009 financial reporting. The intention is to improve the working relationship with companies and thereby to increase the effectiveness and efficiency of the supervision, which in turn will improve the quality of financial reporting. The AFM will of course take formal action where required.

In its follow-up reviews, the AFM has, by way of experiment, taken an informal approach. 19 of the 21 companies approached cooperated in the reviews. Six undertook to make improvements to their financial reporting in the subsequent year. Two of the companies stated they did not agree with the opinion of the AFM. The AFM accordingly decided to issue a request for further information and a notification. In 13 of the financial statements reviewed, the notifications were complied with. The percentage of companies complying with the notifications they received in the preceding year fell slightly, from 75 to 70 percent.

In 2010 the AFM completed 42 (2009: 39) full desktop reviews. The number of requests for further information fell slightly from 38 in 2009 to 36 in 2010. The number of companies receiving a notification or recommendation after completion of a full desktop review fell from 30 in 2009 to 26 in 2010. This was mostly due to the fact that reviews dating from 2009 had not been formally completed. A recommendation was issued to three companies (2009: one).

[2] The follow-up review investigates the extent to which the AFM's notifications have been complied with regarding the annual reports for the previous financial year.

In one of these three cases the enforcement term[3] had already expired, however a new term[4] of a further six months had started because the shortcoming did not appear in the financial statements. Two of the companies which received a recommendation do not have a market listing in the Netherlands.

No recommendation was issued with regard to two financial statements because the six-month enforcement term had expired, although this was justified on the basis of non-compliance with reporting requirements identified. One company ignored the AFM's request to voluntarily publish a press release. In the other case it is not known whether the company will voluntarily cooperate. The extension of the enforcement term from six to nine months that was adopted by the Lower House in December 2010 will, once it is adopted by the Upper House, relieve the situation.

The provision of information on financial instruments by financial institutions in their financial reporting, such as the maturity analysis of financial liabilities, has improved. The disclosures requiring improvement are those associated with financial instruments for which the fair value is not determined on the basis of observable market data, with reclassifications, and with financial instruments designated for valuation at fair value with changes in value recognised in the income statement. This also applies to the division of time bands in the maturity analysis.

As a result of the investigative report by Anton R. Valukas on the bankruptcy of Lehman Brothers, in its letters to financial institutions requesting further information the AFM also asked whether prior to the end of 2009 they had conducted similar (repo) transactions. For the AFM, there was no reason based on publicly available facts or circumstances to doubt that the financial reporting requirements had been correctly applied. This was confirmed in all cases. All financial institutions provided the information requested, although there were some critical reactions. The information received gave no further reason to doubt that the financial reporting requirements had been correctly applied.

In view of the interest in these assets, in 2011 the AFM will focus on the reporting and risks of exposure to government bonds issued by countries with a higher credit risk. The AFM will take the same approach in these cases as it has with repo transactions, if necessary.

In 2010 the AFM focused on the requirement of general publication and simultaneous filing of the financial reporting with the AFM. In order to prompt companies, especially bond funds, to comply with these requirements, the AFM issued 72 instructions. Some bond funds have not yet complied with the instruction. It is a positive development that the general publication and filing of interim statements by the equity funds is progressing satisfactorily. One aspect that can be improved is that publication and filing of the financial reporting with the AFM should be *simultaneous*. The AFM notes that filing is often delayed, especially in the case of the annual financial reporting. The AFM will

[3] For a period of six months after adoption of the financial statements, the AFM has the option of submitting a request for information or review to the Enterprise Chamber. See Section 2:449(1) BW and Section 2:452(2) BW.
[4] Based on Section 2:449(4) BW, a new enforcement term of a further six months commences in the event that a shortcoming does not appear in the financial statements.

enforce this requirement more rigorously in 2011. In conclusion, the AFM once again appeals to companies to file their financial reporting in PDF format at the AFM's digital portal [hereinafter, Loket AFM].

Approximately 275 companies filed their annual and semi-annual financial reports with the AFM in 2010. Approximately 150 companies (equity funds) filed an interim statement with the AFM in the second and fourth quarters.

A small number of companies apply the consolidation exemption for intermediate holding companies[5], whereby they are not obliged to prepare consolidated financial statements based on IFRS. The fact that listed companies can apply this exemption is in conflict with the 7th EC Directive. The AFM has urged the Ministry of Finance to change the law, and calls on companies to cease using this exemption. Companies that are not obliged to prepare consolidated financial statements can prepare very summary annual documentation that is not audited, subject to certain conditions[6]. Although the application of this exemption by listed companies leads to less transparency, particularly if the parent company is not listed, the legislative history of the Financial Supervision Act [*Wet financieel toezicht*, or Wft] does not address this concurrence. In February 2009 the AFM published its position on its website that companies applying this exemption only had to publish and file their summary annual documentation[7]. The AFM is currently reconsidering its position and is in consultation with regard to a possible change to the law.

In its letter relating to the legislation, the AFM noted that the existence of Chinese Walls and its limited powers for the supervision of financial reporting were obstacles. The International Monetary Fund (IMF) recommended in 2010 that the AFM should be given the right to ask questions regarding the correct application of the reporting requirements[8]without having to establish the existence of doubt on the basis of publicly available facts or circumstances. In addition, according to the IMF, the AFM should be able to demand specific documents and/or information.

The follow-up thematic review of semi-annual financial reporting in 2010 shows that transparency for investors has improved since 2009. The disclosures on acquisitions in particular showed a marked improvement in 2010. The disclosures relating to the identification of risks in the remaining six months could be further improved. The semi-annual statement should be a document that can be read in isolation, and therefore reference to the financial statements in the previous reporting year would seem to be inadequate. The regular desktop reviews of the semi-annual statements did not lead to a request for information or a notification.

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[5] See Section 2:408 BW.
[6] See Section 2:403 BW.
7 *http://www.afm.nl/nl/professionals/diensten/veelgestelde-vragen/transparantierichtlijn/financiele-verslaggeving.aspx?perpage=10* (only available in Dutch)
[8] Based on Section 2(1) Wtfv, the AFM can request further disclosure if on the basis of publicly available facts or circumstances it has doubts regarding the correct application of the reporting requirements.

In conclusion, it can be said that the AFM has been very active internationally in its efforts to promote the international consistency of enforcement and the quality of the new financial reporting standards.

2 Introduction

The AFM published most of the findings from its desktop reviews and thematic reviews in 2010 in 'Items of Attention in Financial Reporting for 2010' on 2 November 2010. By publishing its findings at an earlier stage, the AFM expects companies to take note of the items where improvement is required in the preparation of their financial reporting for 2010. The Activity Report for 2010, which is now less extensive, gives an account of the activities carried out by the AFM in the context of its supervision of financial reporting with the help of a number of statistical summaries and notes. As was the case in 2009, brief attention is devoted to the developments in relation to the limited powers of the AFM with regard to supervision and the Chinese Walls problem. Certain findings are also mentioned which were not adequately described in 'Items of Attention in Financial Reporting for 2010'.

Partly on the basis of signals from the market, the AFM has made an effort to improve its communication and working relationship with the companies subject to its supervision. The AFM made changes to the language and tone of its communications in 2010, and by way of experiment took a less formal approach in its follow-up reviews.

3 Annual financial reporting

3.1 General

10 percent more reviews completed
In its supervision of compliance with the reporting requirements, the AFM distinguishes two types of desktop reviews: full desktop reviews and follow-up reviews. Based on a risk analysis, notifications in relation to financial reporting for previous years and rotation, the AFM selected the annual financial reporting of 90 companies: 59 full desktop reviews and 31 follow-up reviews. The AFM did not receive any 'public' signals in 2010 that gave reason to suggest that annual financial reporting that had not been selected should be selected for a desktop review. In two cases however the annual financial reporting of companies selected for a follow-up review were fully reviewed because 'public' signals gave reason to do so. In one case, the signal was only available after the follow-up review had been completed. These financial statements were therefore subjected to two reviews.

In 2010 the AFM initiated desktop reviews of the financial reporting of 67 (2009: 63) companies: 40 full desktop reviews and 27 follow-up reviews. The financial reporting selected on the basis of rotation was mostly not subject to a desktop review. 61 of the reviews started in 2010 have been completed. Eight (2009: 8) desktop reviews were also completed that had been started in 2009. These mainly related to the annual financial reporting for 2008. A total of 69 (2009: 63) reviews were completed.

Less formal conclusion of the remaining work from 2009 leads to improved financial reporting for 2009

Four of the reviews remaining from 2009 were concluded by the AFM after the written and/or verbal explanation. The reason for this was the limited time period still remaining before the date on which the financial reporting for 2009 had to be published. It was agreed with the companies that they would take account of the AFM's findings when preparing their financial reporting for 2009. These agreements were confirmed to the companies concerned in writing. The follow-up reviews in 2010 revealed that the quality of the financial reporting for 2009 had improved in comparison to 2008, because account had been taken of the AFM's findings as mentioned. The findings in these reviews are not included in the summary included in Appendix A 'Main Issues for Notifications and Recommendations per IFRS standard'. From the reactions from the companies concerned, the AFM understands that this approach is appreciated. Some of the reviews in the remaining work at year-end 2010 will be completed in the same way.

Follow-up reviews are now less formal, which has led to a positive response. Compliance with notifications in the financial reporting for 2009 was not as good as in the reporting for 2008

The financial reporting of 35 companies was designated for a follow-up review in 2010. This review was actually carried out in 27 cases (2009: 24). In these follow-up reviews, the AFM experimented with taking a less formal approach, whereby in case of uncertainty, the AFM first telephones the designated contact persons and later contacts them by e-mail. These are usually members of staff, and not the CFO. Companies were approached in this way in 21 of the 27 cases and the AFM requested further clarification. These requests are reported under the informal activities listed in Appendix A as 'Enquiries'. In 13 of these cases the notifications had been adequately observed. Together with the six cases in which it was immediately clear that the notifications had been adequately observed, the number of financial statements reviewed in which the notifications had been adequately observed came to 19, or 70 percent (2009: 18, or 75 percent). The percentage of companies that adequately observed the notifications declined slightly by five percent. From the point of view of the users of the financial reporting, it is desirable that all notifications are observed by the reporting companies.

Six companies made a commitment to the AFM in the informal phase that the notifications would be adequately observed in the financial reporting for 2010. These commitments were confirmed by the AFM in an e-mail to the contact person, with a copy sent to the CFO. In Appendix A 'Overviews of the supervisory activities' these confirmations are included in the informal activities as 'Agreements'. These 'agreements' are not included in the summary 'Main Issues for Notifications and Recommendations per IFRS standard'. In two cases the AFM did not obtain such a commitment, and therefore the AFM reverted to the formal approach and issued a notification.

The reaction by the companies to this 'informal' approach was positive. For the AFM, this is reason to continue the approach in 2011.

The financial reporting of eight selected companies was not subjected to a follow-up review. Three companies did not produce further financial reporting due to bankruptcy, and five were selected for a full desktop review, four on the basis of the risk analysis and one on the basis of a signal. The observance of the notifications was included in the context of these desktop reviews. The degree of observance of the notifications was no different from that observed among the previously mentioned 27 companies.

Fewer requests for additional disclosure, fewer notifications but more recommendations as a result of the desktop reviews

The AFM completed 42 (2009: 39) full desktop reviews in 2010. A request for additional disclosure was made to 36 (2008: 38) of the companies regarding the application of the reporting requirements. Ten (2009: two) of these companies removed our doubts regarding the correct application of the reporting requirements. The AFM sent one or more *notifications* to 26 (2009: 30) other companies, either accompanied by a recommendation or not. Compared to 2009 this is a decrease of four, or 13 percent, with an eight percent increase in the number of reviews. It should be noted that the decrease was entirely due to the less formal approach taken to completing the remaining work from 2009.

Three (2009: one) notifications were accompanied by a *recommendation* requesting the company to publish a press release stating the effect on the issuer's financial reporting if the reporting requirements had been applied correctly. It should be noted that two recommendations related to the financial reporting of a Dutch entity with a listing only on a European securities market outside the Netherlands.

New enforcement term if shortcoming does not appear in the financial statements

Based on Section 2:449(4) BW, a new enforcement term of a further six months commences in the event that a shortcoming does not appear in the financial statements. This term commences on the date on which the AFM could no longer reasonably be unaware of the shortcoming in the financial statements. In one of the three recommendations issued, the AFM issued the recommendation after the original enforcement term of six months had expired on the basis of its option of appealing to this provision.

Recommendations not issued because the enforcement term had expired

In two cases in 2009 (2008: four) the AFM did not issue a recommendation with its notification although this was justified in view of the deviations from the reporting requirements that were identified. In both cases, the statutory enforcement term of six months had expired. In these situations, the AFM insisted that the issuer should publish a press release on its own initiative. One issuer indicated that it was not prepared to do so, and at the time of publication of this activities report it was not known whether the other issuer concerned was prepared to do so. This shows that the extension of the enforcement term from six to nine months recently approved by the Lower House is more than welcome to both the AFM and to investors. See section 6 of this report.

No review procedure put before the Enterprise Chamber

As in previous years, all the recommendations made by the AFM resulted in the publication of a press release that was included in the AFM's Financial Reporting Register. The AFM did not encounter any inadequacies in the financial reporting that justified an immediate recourse to the Enterprise Chamber without a recommendation being made to the company concerned[9]. As was the case in 2007, 2008 and 2009 and in view of the above, the AFM did not put any review procedures before the Enterprise Chamber in 2010. An important observation is appropriate in this respect: the AFM's limited powers in this area of supervision, in particular the requirement that its doubts must be based on publicly available facts and/or circumstances, imply a risk that the AFM has not been able to detect all the issues related to reporting. This risk is highest with regard to inaccuracies in the measurement of balance sheet items. Moreover, the AFM cannot force the company to submit specific documents and/or information. This limits the AFM's ability to investigate the matter, and in some cases makes it difficult to establish whether a recommendation is justified.

Appendix A contains a table listing the activities relating to supervision with regard to compliance with the reporting requirements. This table takes no account of requests for additional information and notifications issued in connection with the thematic reviews.

3.2 Recommendations and notifications

General

The AFM has published its provisional findings from the desktop reviews and the thematic reviews in the 'Items of Attention in Financial Reporting for 2010'. This section of the Activity Report deals exclusively with the areas of improvement not mentioned in this publication. There is also a comment to be made regarding the results of the thematic review of 'Operating Segments' (IFRS 8). The report does not state that with effect from the 2010 financial year the statement of the measure used for the valuation of the total of the assets and liabilities of a segment only needs to be included if the chief operating decision maker is regularly informed in this respect.

Recommendations

With regard to the elements of the financial reporting for which the AFM issues a recommendation, the AFM is of the opinion that correct application of the reporting requirements has an important effect on the company's financial reporting, now and in the future. For users of financial reports, it is important that they are immediately aware of this so that they are in a position to make properly considered investment decisions. The publication of a press release in relation to a recommendation ensures that this transparency is achieved. The recommendation thereby contributes to the proper functioning of the capital markets and investor confidence in these markets. The AFM's view is that greater transparency with regard to these elements outweighs any interest the issuing institution may have in not going public.

The AFM issued three (2009: one) notifications accompanied by a recommendation in 2010. One recommendation concerned the financial reporting for 2008 and two concerned the financial reporting for 2009.

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[9] Based on Section 4(2) Wtfv the AFM can submit a request for review to the Enterprise Chamber in the interests of the proper functioning of the securities market or the position of investors after it has issued a notification without a recommendation.

The recommendations made by the AFM relate to:

- The disclosure relating to a reported impairment. The disclosure did not include the breakdown of the loss per cash-generating unit and the description of the circumstances that led to the impairment;
- The method of determining the fair value of financial instruments. The company had applied its own measurement model (level 3 valuation) although price quotations in an active market (level 1 valuation) were available for the financial instruments in question;
- The way in which the effects of business combinations were included in the cash flow statement and in the disclosures relating to business combinations. The cash acquired as a result of the business combination were incorrectly classified in the cash flow statement and not separately disclosed. Moreover, there was no description of the main factors contributing to the payment of goodwill as well as the amounts of the main categories of assets and liabilities in the subsidiary companies acquired.

In two of the three recommendations, the shortcomings did not affect the size and composition of the company's assets and/or result, nor did they affect the size of its operating cash flow. A number of relevant disclosures were lacking so that a proper estimation of the future cash flows was difficult if not impossible.

Notifications

More notifications regarding associates

It is notable that the number of notifications regarding the application of the reporting requirements for associates (IAS 28) rose from one in 2009 to five in 2010. The notifications relate to different elements of the standard. The incorrect applications include the failure to include an impairment, the statement of an incorrect valuation principle and the failure to disclose the refutation of the possibility of the existence of an associate. The summary financial information of the associate, including the total of its assets, liabilities, income and result, was also missing. Lastly, in one set of financial statements, depreciation on part of the assets of the associates was reported under depreciation.

Significantly fewer notifications regarding the application of the provisions in Part 9 Book 2 BW

The AFM issued 12 notifications (2009: 33) regarding the incorrect application of the reporting requirements in Part 9 Book 2 BW. Nine of these notifications related to the separate financial statements (2009: 26). In most cases, this concerned the incorrect application of the equity method for the valuation of consolidated group companies. Apart from one single exception, companies apply the provisions in Part 9 Book 2 BW in their separate financial statements and use the IFRS accounting principles they use in their consolidated financial statements[10]. The principle for consolidated associates stated in the consolidated financial statements is not applicable in the separate financial statements. This means that the company must use the principle stated in Section 2:389(2) BW of the net asset value based on asset movements. The companies reviewed that had applied the

[10] Based on Section 362(8) BW a company that has prepared its consolidated financial statements on the basis of IFRS may apply the same accounting principles it used in the consolidated financial statements in its separate financial statements.

equity method have given a commitment to apply this accounting policy in their financial reporting for 2010.

3.3 Semi-annual financial reporting

For a limited review of the semi-annual financial reporting, statements were selected of companies which were or are subject to a full desktop review for the preceding year. A number of press releases were also studied at the request of the division responsible for the supervision of market abuse. Lastly, the AFM selected certain semi-annual statements for a limited review on the basis of signals indicating potential problems in the semi-annual financial reporting.

Requests for information, but no notifications in relation to semi-annual financial reporting
The AFM initiated a limited review for 40 semi-annual statements, some of which still have to be completed. The reviews conducted led to two requests for further information. There was also contact by telephone in some cases. No notifications were issued.

3.4 Financial reporting by financial institutions

Quality of financial reporting by financial institutions has improved, but further improvement is required
The AFM also subjected the financial reporting of a large number of financial institutions to a desktop review in 2010. These desktop reviews and the thematic review conducted show that the provision of information regarding financial instruments has improved in comparison to the previous year, but that further improvement is necessary. The notifications issued by the AFM with regard to previously conducted desktop reviews had a positive effect on the quality of the financial reporting. The changes to IFRS 7 in 2008 and 2009 may also have contributed to this improvement.

In previous years the AFM asked numerous questions and issued notifications regarding the maturity analysis of the financial liabilities, in which the remaining contractual maturities are shown. This mainly concerned the failure to state non-discounted amounts, the failure to include financial liabilities arising from future interest payments and the failure to provide a maturity analysis for each financial liability. With one exception, compliance is now satisfactory with respect to these items. The AFM does however note that not all financial liabilities have been classified by time band, although this is a requirement. There is still room for improvement here.

The summary of movements for financial instruments for which fair value is not determined on the basis of observable market data (level 3) is not provided in all cases. Moreover, the fair value profits and losses that would be included in the result or equity if reclassification had not occurred and the profit, the loss, the income and/or expense recognised in the income statement in the reporting year are not stated in all cases. Lastly, in some cases, specific information is missing with regard to loans and receivables and financial liabilities designated as measured at fair value with recognition of value changes in the income statement. These disclosures require further improvement.

We also refer to the findings of our thematic review of IFRS 7 published in November 2010. With regard to financial institutions, the AFM's focus in 2011 will be on the reporting and risks related to the exposure to government bonds issued by countries in Southern Europe and Ireland.

Financial institutions provide information in response to questions regarding the conduct of repo transactions, although there is no reason for concern at the AFM on the basis of public information
The report by Anton R. Valukas investigating the bankruptcy of Lehman Brothers Holdings Inc. was published in March 2010. The report shows that Lehman used repo transactions (105 and 108) as a result of which securities were removed from the balance sheet immediately before the end of a reporting period and returned to the balance sheet immediately after the beginning of the subsequent reporting period. According to the researchers, this led to a misleading picture of the financial position of Lehman at the end of 2007 and in 2008. As a result of this publication, various European regulators have checked to establish the extent to which European financial institutions had conducted similar transactions. In view of the special interest of the users in such forms of 'window dressing', the AFM also investigated this issue further. In its letters requesting further information, the AFM also asked whether the financial institutions had conducted such transactions prior to the end of 2009, even though there was no reason on the basis of public information or circumstances for the AFM to suspect that the financial reporting requirements had not been correctly applied. In cases where there is no legal basis for putting a question, the AFM makes this clear. All financial institutions provided the information requested, although there were some critical reactions. The AFM is pleased with the cooperation, but wonders whether this would have been the case if the reporting requirements had not been correctly applied.

The AFM's focus with regard to financial institutions in 2011 will be on the reporting and risks related to the exposure to government bonds issued by countries in Southern Europe and Ireland. This is an issue of great interest to investors. In view of the level of attention, the AFM will also request information in cases where there are no doubts regarding the application of the reporting requirements.

4 Other activities

This section of the Activity Report gives a summary of the other activities of the AFM relating to its supervision of financial reporting. Attention is then paid to the changes made by the AFM in its requests for additional information, its international activities and its contacts with the Financial Reporting Committee.

4.1 Requests for further information

Less formal approach to requests for further information
The AFM tried to make its requests for further information more understandable and accessible in 2010 by using simpler language and taking a less formal approach. From the reactions in the market, the AFM understands that the less formal tone in its letters is appreciated, but that further improvements are possible. The AFM is trying to take a still less formal approach and thus increase the effectiveness and efficiency of its supervision. For this reason, the 'Appendix II Comments' will no longer be attached to the request for

further information with effect from 2011. This appendix consisted of a list of the points noted by the AFM during its assessment of the financial reporting and its comments that it expected to be taken into account in the preparation of future financial reporting. Another feature of the less formal approach is that the AFM addresses its requests for future information to the CFO of a company rather than its executive board. Furthermore, in case of areas of uncertainty in the financial reporting we normally attempt to contact the company on an informal basis before issuing a request for further information.

After the successful test of the companies in the AEX, since 2010 all companies are notified one to two weeks in advance that they can expect to receive a request for further information. The AFM is also proposing to extend the standard response time from 10 to 20 business days. The extended response time will come into effect as soon as the parliamentary bill to extend the current six-month term[11] by a further three months becomes law[12].

In response to requests from the market the AFM has decided to issue its requests in English with effect from calendar year 2011 in cases where the adopted financial statements are not prepared in Dutch.

4.2 International activities

The AFM has actively participated in CESR-fin[13], also through its participation in the eight EECS (European Enforcement Coordination Sessions) meetings. At these meetings the European regulators discuss the supervisory decisions relating to financial reporting made by one of their number, including ten decisions made by the AFM. The AFM also submitted two complex cases before making a decision. The purpose of EECS is to achieve and ensure a consistent application of IFRS in Europe. The AFM is a member of the agenda committee of EECS.

The AFM also participated in the CESR-fin project groups ‘CESR-fin on IFRS’ and ‘CESR-fin on fair value accounting’. The first of these project groups is permanently constituted and writes commentary letters to the International Accounting Standards Board (IASB) and European Financial Reporting Advisory Group (EFRAG) on the basis of Discussion Papers (DP) and Exposure Drafts (ED) of accounting standards. In its assessment of a DP or ED, CESR (now known as ESMA, see footnote 13) primarily focuses on the question of whether the proposals will lead to relevant information being provided to investors and the extent to which the correct application of the proposed reporting requirements is enforceable by the regulator. The AFM was one of the authors. Important EDs commented on in 2010 include:

[11] For a period of six months after adoption of the financial statements, the AFM has the option of submitting a request for information or review to the Enterprise Chamber. See Section 2:449(1) BW and Section 2:452(2) BW.
[12] The bill in which this will be arranged was adopted by the Lower House at the end of November 2010. The Upper House is expected to make a decision on the bill in the near future.
[13] CESR was reformed to become the European Securities and Market Authority with effect from January 2011.

1. ED Financial Instruments: Amortised Cost and Impairment (IFRS 9);
2. ED Conceptual Framework: the Reporting Entity;
3. ED Revenue from Contracts with Customers;
4. ED Lease Contracts; and
5. ED Insurance Contracts.

In early 2010 the AFM led a CESR-fin project that conducted a technical analysis of IFRS 9 Financial Instruments: Classification and Measurement at the request of the European Commission.

The project group 'CESR-fin on fair value accounting' issued a report on compliance with the provision relating to the provision of information on financial instruments (IFRS 7) in the 2008 financial reporting of 96 European financial institutions in November 2009. The report shows that the disclosures need to be improved in certain respects, including the method of determination of the fair value and the assumptions used in this process. This information is important for a proper understanding of an issuer's financial position and performance and can therefore affect the decisions made by users.

In 2010 the project group conducted a follow-up review to establish the extent to which the information provided on financial instruments in the 2009 financial reporting had improved. The report[14] published on 26 October 2010 shows that these disclosures have improved in all respects in comparison to the financial reporting for 2008. The disclosures in relation to valuation techniques, 'own credit risk', 'day one profits', and 'special purpose entities' had significantly improved. The project group also notes that the fair value hierarchy (levels 1, 2 and 3), which is compulsory with effect from the financial reporting for 2009, was properly disclosed. In conclusion, the financial institutions were urged to further improve their disclosures. The situation at the Dutch financial institutions is no different from that described in both CESR reports.

4.3 Financial Reporting Committee

Also in 2010, the AFM had three meetings with the Financial Reporting Committee (the 'Committee'), an advisory body consisting of experts (academics, accountants, lawyers, users and compilers of financial reporting) in the area of financial reporting. At these meetings, items relating to the supervision of financial reporting were discussed. This year the topics discussed included the AFM's limited powers, the Chinese Walls and the application of Section 2:403 BW and Section 2:408 BW by listed companies. The AFM also asked the Committee for advice on its thematic reviews in the 2010 reporting year and on complex reporting issues in supervision cases.

One of the Committee members, Prof. Leo (L.G.) van der Tas, has been appointed a member of the Consultative Working Group, an advisory body for CESR-fin on the nomination of the AFM.

There was one vacant seat on the Committee at the end of 2010.

[14] http://www.afm.nl/nl/professionals/afm-actueel/nieuws/2010/nov/cesr-disclosures.aspx

4.4 The view of companies and investors of the supervision of financial reporting

Companies think that the AFM has a good understanding of IFRS, that this is being applied properly and that there is openness in the verbal communication
The AFM has had extensive discussions with two representatives of the Financial Reporting Committee regarding how investors and companies subject to supervision view the supervisory process and where they see room for improvement. The contribution from one of the Committee members was based on a survey of CFOs of a number of listed companies. The positive responses regarding supervision mentioned by respondents concerned the good knowledge of IFRS, the fact that the supervisors are asking the right questions, and the fact that their comments are technically correct in most cases. Other points mentioned were the openness of the verbal communication and the cooperative attitude of the AFM in the setting of deadlines. The reports on the thematic reviews and the annual activity report were also appreciated.

Companies think the AFM is too formal and legalistic, that it acts on the basis of mistrust rather than trust and that it focuses too much on (insignificant) requirements to provide information
The survey also reveals certain areas where the AFM has to improve. Especially in its written communication, the AFM comes across as too formal. Some companies mentioned a discrepancy between a positive tone in the discussions and the tone used in the letters. The AFM is also accused of focusing on less important issues and designing its desktop reviews to establish that all kinds of (petty) requirements to provide information have been met. Some of the respondent companies felt that the AFM operates on the basis of mistrust rather than trust. A few companies thought that the fact that the AFM did not conduct its correspondence in English was 'unprofessional'.

It has to be remembered that the AFM is a supervisor that strives to achieve transparency for investors. It is therefore highly likely that differences of opinion will exist regarding what is important and what is not. It should be noted that, as a supervisor, the AFM will if necessary act against companies that fail to properly apply the reporting requirements and that give the impression they are not prepared to cooperate.

Investors want more contact, a more thematic approach in the desktop reviews, and fewer technical reports
The users of the financial reports say they think that the AFM should take a more thematic approach by making its desktop reviews less comprehensive and more focused on a limited number of themes, some of which should be announced in advance. Another recommendation was to intensify contacts with investors and make the reports more readable by using less IFRS language. The report on the thematic review of the semi-annual financial reporting was seen as a step in the right direction.

The AFM notes this criticism and will try to improve in this area. The changes already made include the different tone and language in the requests for information and the informal process in the follow-up reviews. Furthermore, with effect from 2011 the AFM will write its letters in English if the addressee's financial statements are not prepared in Dutch. The AFM is currently considering what other improvements it could make, including the question of whether the effectiveness and efficiency of the supervision would be improved if the desktop reviews were more theme-based, with a focus on a limited number of subjects, some or all of which would be announced in advance. Lastly, we will investigate how we can intensify our contacts with investors and how we can increase the readability of our reports.

5 Findings from the supervision of publication and filing of annual and semi-annual financial reporting and interim statements

5.1 Publication and filing

One of the obligations for companies subject to regulation is to publish the annual and semi-annual financial reporting within 4 and 2 months of the end of the respective reporting period and simultaneously to file a copy with the AFM[15]. Companies with shares listed on the stock exchange have to publish an interim statement in the period lying between 10 weeks after the beginning and 6 weeks before the end of the half year and simultaneously file a copy with the AFM[16]. The AFM focused on compliance with this obligation in 2010.

AFM request for filing of financial reporting in PDF format
Companies can file the copies of their semi-annual or annual reports and/or interim statements in two ways: as a PDF file at Loket AFM or in hard copy form by post, using the form for the filing of periodic information that is available on the AFM's website. Electronic filing is quick and easy. A large majority of companies have taken advantage of this option. The AFM encourages all companies to file their financial reporting in electronic form.

In past years, the AFM has noted that compliance with the requirement to publish the financial reporting and file it simultaneously with the AFM needed to be improved. Most of the infringements were committed by companies that had only issued bonds listed on the stock exchange. The AFM focused on compliance with this obligation in 2010, by sending a reminder letter to companies and/or an instruction if they had not complied with this obligation on the last due date of filing with the AFM.

Filing and publication of financial reporting should always be simultaneous
In 2011 the AFM will again focus on compliance with the requirement to publish financial reporting and simultaneously file it with the AFM. Attention will also be paid to establishing that the filing of reports takes place at the time of publication. The AFM has noted that some companies only file their financial reports a few days before the final due date although publication has occurred earlier, in some cases more than a month earlier.

[15] See Sections 5.25c (1) of the Financial Supervision Act, or 'Wft' (annual financial reporting) and 5.25d (2) Wft (semi-annual financial reporting).
[16] See Section 5.25^{e} (1) Wft.

5.2 AFM Public Register of Financial Reporting

AFM no longer treats failure to file financial reports twice (as price-sensitive information and as financial reporting) as an offence

In addition to its register of financial reporting, the AFM also maintains a register of price-sensitive information. Much of the material in financial reporting, especially the semi-annual reports and the interim statements, also qualifies as price-sensitive information and therefore has to be included in *both* these registers. The registers have different access points, with separate enquiry forms: the portal for price-sensitive information [the PSI portal] and the portal for financial reporting [Loket AFM]. Companies were obliged by the AFM to submit what was usually the same message twice. Partly as a result of signals from the companies, the AFM changed its policy in this respect in 2010. Companies must in any case submit their financial reporting via the PSI portal if it qualifies as price-sensitive information. In these cases the AFM asks companies to also submit their financial reporting via Loket AFM because in the context of its supervision it needs certain further information that companies cannot yet provide in the form used for the PSI portal. In case a company submits its financial reporting only via the PSI portal and provides the additional information for the financial reporting register (possibly at the request of the AFM), the AFM assumes that the filing obligation has been met. We are currently working on an IT solution so that the additional information for the financial reporting register can also be provided in the enquiry form used for the PSI portal.

On balance 72 instructions, mostly for bond funds, not all of which have been complied with

In May 2010 the AFM sent a total of 89 instructions to companies that had not published their financial reporting, or had not filed their published financial reporting with the AFM via Loket AFM. Of the 89 instructions, 73 (49 for bond funds and 24 for equity funds) related to the annual financial reporting and 16 to the interim statements. As a result of the changed policy regarding the twofold filing and the fact that a number of bond funds had not selected the Netherlands as their member state of origin, 28 instructions were withdrawn so that 61 remained. Of these 61 instructions, 38 were complied with. The financial reporting of a number of bond funds is still not included in the financial reporting register. Making contact in these cases is proving to be extremely difficult.

In the second half of the year, the AFM changed its approach, in the sense that it now sends a reminder letter in the first instance and then issues an instruction if this has no effect. 48 reminder letters were issued, of which 44 (37 bond funds and 7 equity funds) related to the semi-annual financial reporting, and 4 to the interim statement. Instructions were sent to one equity fund and ten bond funds because the semi-annual report had not been published and had not been filed with the AFM after the reminder letter had been sent.

Publication and filing of the interim statements is progressing satisfactorily and requires minimal supervisory action

More than 150 equity funds are obliged to file an interim statement twice a year. In the first and second halves of the year, the interim statements of six and four companies respectively were not published and filed in good time. After the AFM had sent an instruction or a reminder letter these companies complied with their obligations.

What is included in the Financial Reporting Register in 2010

Approximately 275 companies filed their annual and semi-annual financial reports they had published with the AFM in 2010. Approximately 150 companies (equity funds) published an interim statement and filed this with the AFM in the second and fourth quarters. The AFM issued three recommendations in 2010; one related to the 2008 reporting year, and two to the 2009 reporting year. As a result of the recommendations, these three companies published a press release regarding their financial reporting and filed this with the AFM. The press releases were included in the Financial Reporting Register.

5.3 Application of the exemptions in Section 2:403 BW and Section 2:408 BW

Consolidation exemption for interim holding companies should not be applicable by listed companies. Appeal to remove the application of this exemption

Section 2:408 BW in Part 9 Book 2 provides the possibility of not issuing consolidated financial statements, subject to certain conditions being met. Contrary to the provision in the 7th EC Directive, this exemption can also be applied by companies that have quoted shares outstanding. This conflict with the 7th EC Directive means that on the basis of this exemption, listed interim holding companies have no obligation to apply IFRS. A small number of companies are using this option and not preparing consolidated financial statements according to IFRS. In some cases the consolidated IFRS financial statements of the parent company, which is not subject to regulation by the AFM in all cases, are included as an appendix to the separate financial statements of the interim holding company.

From the point of view of transparency for investors, the AFM does not consider it desirable that interim holding companies should be able to make use of this exemption. The AFM has urged the Ministry of Finance to amend Section 2:408 BW so that this exemption for listed interim holding companies would be removed. In the interim, it urges interim holding companies to refrain from applying this exemption.

Subject to certain conditions, group companies can make use of the exemptions stated in Section 2:403 BW. These exemptions allow a company to prepare only a summary balance sheet and income statement, with no disclosures, annual report and other data. Audit and publication of these documents is not compulsory. An important condition allowing the use of this exemption is that the parent company, which does not necessarily have to be a listed company, accepts joint and several liability for the liabilities of the group company making use of these exemptions.

The application of this exemption is directly contrary to the intention of Section 5.1a 1.2 Wft, periodic obligations for issuers. This section states that listed companies must publish their annual financial reporting within four months of the end of the reporting year and simultaneously file a copy with the AFM[17]. In the drafting of this section of the Wft, no account is taken of the possibility that listed companies could apply this exemption. After consultation with the Ministry of Finance, the AFM has accordingly taken the position that the obligation to publish the annual financial reporting applies after taking account of the exemptions in Section 2:403 BW. This means that only the 'true and fair view declaration' and the summary balance sheet and income statement must be published and simultaneously filed with the AFM. The AFM published this position on its website in February 2009.

Opinions in the literature regarding this policy vary. In Ireland and Luxembourg, where the reporting legislation contains a similar exemption, the provisions of securities law prevail and issuing institutions may not make use of the exemption. These facts and circumstances have led the AFM to reconsider its position and to consult with the Ministry of Finance. We are currently studying the extent to which the law and the AFM's policy should be changed. The AFM can envisage a situation in which the exemptions remain in effect, but the periodic obligations for issuers are transferred to the parent company that has accepted joint and several liability for the obligations of the listed group company.

For the sake of completeness it should be noted that Section 2:403 BW does **not** apply to semi-annual financial reporting and may not be applied in this respect. This does not conflict with the position taken by the AFM to date.

6 New development regarding limited powers of the AFM, Chinese Walls and the enforcement term

In Section 6 of the 2009 Activity Report[18] published in December 2009 the AFM devoted extensive attention to the problems raised by Chinese Walls and the limited powers of supervision at its disposal. In this section the AFM describes the relevant developments in these areas occurring in 2010.

In its letter relating to the legislation, the AFM requested more powers and the removal of Chinese Walls

Based on input from the AFM and DNB in their first letter relating to the legislation, in October 2010 the Minister of Finance informed the Lower House with regard to the difficulties the regulators had identified in the regulations. The items mentioned included the lack of powers regarding the supervision of financial reporting and the presence of Chinese Walls. The strengthening of powers envisaged mainly consisted of the ability to request further information regarding the application of the reporting requirements without the necessity of doubt regarding the correct application of the rules based on publicly available facts or circumstances, and the power to demand that specific information and/or documentation should be provided. The extension of powers is necessary in order to be

[17] Section 5:25c Wft.
[18] *http://www.afm.nl/layouts/afm/default.aspx~/media/files/fin-verslag/items-attention-fv-2010-eng.ashx*

able to review aspects of the financial reporting for which there is a higher risk of incorrect application of the reporting requirements and/or which are a matter of great public interest.

The removal of Chinese Walls would enable the exchange of information between the division responsible for the supervision of financial reporting and the other divisions. This exchange of information is necessary for effective and efficient supervision. The AFM envisages that signals from the supervision of audit firms provided to the division supervising financial reporting will remain limited to ‘serious’ reporting issues. It is not our intention that the staff of the financial reporting supervision division should have access to audit files or that they should duplicate the work of the auditor. Furthermore, other divisions should not be permitted to request information for the purpose of the supervision of financial reporting.

The IMF considers an extension of the powers in relation to financial reporting supervision to be desirable

The IMF reviewed the financial supervision apparatus in the Netherlands in comparison to international standards and published its provisional conclusions in autumn 2010. According to the IMF the AFM has an adequate supervisory framework for the financial markets and largely meets the international standards set by the International Organisation of Securities Commissions (IOSCO). The IMF does however point out that certain changes are necessary in order to improve the quality of supervision. One important recommendation is that the AFM’s powers relating to the supervision of financial reporting should be extended. The recommended extension of powers concerns the ability to demand specific information and/or documentation and the authority to ask questions without having to establish the existence of doubt regarding the correct application of the reporting requirements on the basis of publicly available facts and/or circumstances.

Evaluation of the Financial Reporting Supervision Act [Wet toezicht financiële verslaggeving]

In the context of the evaluation of the Financial Reporting Supervision Act [*Wet toezicht financiële verslaggeving*, or ‘Wtfv’] required by law, the University of Tilburg (UvT) was instructed by the Ministry of Finance to establish whether and to what extent the AFM had operated efficiently and effectively in the implementation of the Wtfv. The UvT also studied whether the introduction of the Wtfv had contributed to improving the quality of the financial reporting. The UvT’s report is expected to be published in the near future.

Enforcement term still not extended from six to nine months

As a result of the fall of the Balkenende 4 Cabinet in February 2010, the debate of the bill to extend the enforcement term from six to nine months in the Lower House has been delayed until the end of 2010. At the time of publication, the bill still has to be approved by the Upper House, after which it can be published in the Bulletin of Acts and Decrees [*Staatsblad*]. The AFM expects the new enforcement term to take effect in the current calendar year.

7 Follow-up thematic review of semi-annual reporting for 2009

The AFM published the results of its 2009 thematic review 'semi-annual financial reporting by listed companies'[19] in May 2010. The review showed that transparency in the 2009 semi-annual statements, which is important to investors, had greatly improved in comparison to 2008. The AFM also noted that there was room for improvement in certain respects.

Some of the potential improvements in the semi-annual financial reporting were implemented in 2010. This led to improved transparency for investors. Further improvement is possible.
A follow-up review of the 2010 semi-annual statements was conducted in the second half of 2010, only for the purpose of establishing whether the points the AFM had identified as needing improvement had been disclosed more clearly. These points concerned the disclosure of the major events in the first six months, the disclosure on risks and uncertainties in the remaining six months of the reporting year, the disclosure on significant acquisitions and the Statement of Comprehensive Income (CI) (also known in Dutch as the *overzicht van het totaalresultaat*).

Much improved disclosure of material business acquisitions
The disclosure of material business acquisitions improved greatly in 2010. New reporting requirements for acquisitions were introduced in 2010. This entailed a significant change to the information that has to be provided in connection with an acquisition compared to 2009. In the 2010 semi-annual statements, an acquisition considered to be material had occurred in 13 cases. In all these cases, information on the acquisition was included in the semi-annual statement. In only five cases was the information provided considered to be less than adequate. This is a big improvement compared to 2009, when five companies included information on acquisitions in their semi-annual statement and none of them provided the full information required.

Inclusion of the OCI statement has improved
The amendment to IAS 1 regarding the presentation of the results took effect in 2009. The comprehensive income can be presented either in one statement, or two statements (the income statement and the statement of other comprehensive income, or OCI). An improvement was noted in this respect in 2010, as 93 percent of the companies have now included an OCI in their semi-annual statement compared to 84 percent in 2009.

The disclosure on major events is still not specific enough
The disclosures on the significant events in the first six months were still not sufficiently specific. An improvement in the disclosure of events in the first six months was noted in only one case.

[19] *http://www.afm.nl/layouts/afm/default.aspx~/media/files/fin-verslag/items-attention-fv-2010-eng.ashx*

Many companies refer to the annual financial report in their disclosure on risks and uncertainties

All the companies provide a disclosure regarding the risks and uncertainties in the remaining six months of the financial year, although the description of risks is less extensive. In 2010, only 65 percent of the companies (2009: 70 percent) gave a full description of the risks and uncertainties in the remaining six months of the financial year. The other companies refer to the corresponding disclosure in the last annual financial report, in some cases with a further statement that these risks have not changed.

Appendix A: Overviews of supervisory activities[20]

	Total	AEX	AMX	AScX	Local [21]	Abroad [22]
Companies subject to supervision [23]	**296**	**21**	**23**	**23**	**143**	**86**
Remainder from 2009	**8**			**2**	**5**	**1**
Companies selected	**89**	**11**	**11**	**9**	**40**	**18**
Desktop reviews initiated:	**67**	**10**	**10**	**6**	**34**	**7**
Follow-up	*27*	*5*	*5*	*2*	*12*	*3*
Risk analysis and rotation	*39*	*5*	*5*	*4*	*21*	*4*
Signal	*1*	*-*			*1*	
Desktop reviews completed:	**69**	**10**	**10**	**6**	**33**	**8**
Financial statements 2008	*8*	*-*	*-*	*2*	*5*	*1*
Financial statements 2009	*59*	*10*	*10*	*4*	*28*	*7*
Remainder from 2010	**6**	**0**	**0**	**1**	**5**	**0**
Supervisory activities:						
Request(s) for further information	38[24]	7	4	3	21	3
Notifications	25[25]	6	4	1	13	1
Recommendations	3	-	-	-	1	2
Informal activities[26]**:**						
Enquiries	21	5	4	2	8	2
Agreements	6	1	1	1	3	0

[20] The figures in this overview may differ from those stated in the AFM's annual report. Notifications are included in this overview if they are known at the end of the year, whereas the annual report only includes notifications issued during the calendar year.
[21] This concerns Dutch companies and companies from third countries with shares (not included in an index) and/or bonds listed in the Netherlands.
[22] This concerns Dutch companies with shares and/or bonds listed only abroad.
[23] The population of Dutch companies and companies from third countries as at March 2010, to the extent known to the AFM.
[24] Including two follow-up reviews for which a notification was issued.
[25] See footnote 24.
[26] In its follow-up reviews the AFM has experimented with taking an informal approach. See section 3.1.

Main subjects of notifications and recommendations per IFRS standard[27]:

Standard	Brief description	Total	AEX	AMX	AScX	Local	Abroad
IFRS 2	Share-based payment	3				2	1
IFRS 3	Business Combinations	4				3	1
IFRS 4	Insurance Contracts	1		1			
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations	2		2			
IFRS 7	Financial instruments: Disclosures	13	1	2	1	8	1
IFRS 8	Operating Segments	5	1			4	
IAS 1	Presentation of Financial Statements	10	2			7	1
IAS 2/41	(Agricultural) Inventory	2		1		1	
IAS 7	Statement of Cash Flows	8		1		7	
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	2				2	
IAS 10	Events after the Reporting Period	1				1	
IAS 11	Construction Contracts	2	1	1			
IAS 12	Income Taxes	8	1	1		5	1
IAS 16	Property, Plant and Equipment	1				1	
IAS 17	Leases	2				1	1
IAS 18	Revenue Recognition	2		2			
IAS 19	Employee Benefits	6	1	1		3	1
IAS 24	Related Party Disclosures	8		1		7	
IAS 27	Consolidated and Separate Financial Statements	2				2	
IAS 28	Investments in Associates	5		1		4	
IAS 31	Interests in Joint Ventures	1		1			
IAS 32/39	Financial Instruments	7		1		5	1
IAS 33	Earnings per Share	2				2	
IAS 36	Impairment of Assets	10	1		1	7	1
IAS 37	Provisions, Contingent Liabilities and Contingent Assets	2				1	1
IAS 38	Intangible Assets	1				1	
IAS 40	Investment Property	1				1	
SIC 15	Operating leases – Incentives	1				1	
Total		112	8	13	2	79	10

[27] If a standard is mentioned more than once in a notification or recommendation (for instance, regarding different aspects), the standard is still only counted once in this overview. If more than one standard is referred to in a notification or recommendation, each standard is included once. 'Informal' notifications are not included in this overview.

Subjects in BW 2 Part 9 in notifications and recommendations:

Provisions in BW 2 Part 9 concerning:	Total	AEX	AMX	AScX	Local	Abroad
Corporate governance	3				3	
Separate financial statements	9	1	3	1	4	
Total	12	1	3	1	7	0