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International Financial Reporting Standards (IFRS)

An AICPA Backgrounder

The Coming Convergence

The growing acceptance of International Financial Reporting Standards (IFRS) as a basis for U.S. financial reporting represents a fundamental change for the U.S. accounting profession.

Developed by the American Institute of CPAs, in partnership with its marketing and technology subsidiary CPA2Biz, www.IFRS.com provides a comprehensive set of resources for accounting professionals, auditors, financial managers, audit committees and other users of financial statements. Through the Web site, financial professionals can obtain up-to-date financial news and information, CPE and conference training, FAQs, articles and publications, and online video presentations.

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Get Ready for IFRS

The growing acceptance of International Financial Reporting Standards (IFRS) as a basis for U.S. financial reporting represents a fundamental change for the U.S. accounting profession. Today approximately 113 countries require or allow the use of IFRS for the preparation of financial statements by publicly held companies. In the United States, the Securities and Exchange Commission (SEC) has been taking steps to set a date to allow U.S. public companies to use IFRS, and perhaps make its adoption mandatory. In fact, on November 14, 2008, the SEC released for public comment a proposed roadmap with a timeline and key milestones for adopting IFRS beginning in 2014.

The international standard-setting process began several decades ago as an effort by industrialized nations to create standards that could be used by developing and smaller nations unable to establish their own accounting standards. But as the business world became more global, regulators, investors, large companies and auditing firms began to realize the importance of having common standards in all areas of the financial reporting chain.

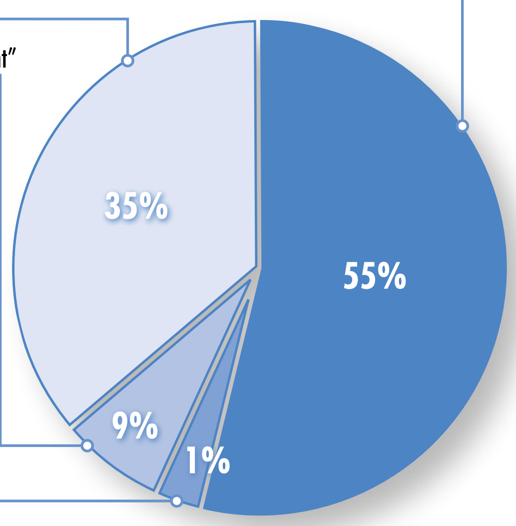
Worldwide Momentum

The globalization of business and finance has led more than 12,000 companies in more than 100 countries to adopt IFRS. In 2005, the European Union (EU) began requiring companies incorporated in its member states whose securities are listed on an EU-regulated stock exchange to prepare their consolidated financial statements in accordance with IFRS[1]. Australia, New Zealand and Israel have essentially adopted IFRS as their national standards. Canada, which previously planned convergence with U.S. Generally Accepted Accounting Principles (GAAP), now plans to require IFRS for publicly accountable entities in 2011. The Accounting Standards Board of Japan (ASBJ) and the International Accounting Standards Board (IASB) plan convergence by 2011. On November 11, 2008, Mexico announced it would adopt IFRS for all listed entities starting in 2012.

IFAC Survey

With respect to the importance of convergence to International Financial Reporting Standards for economic growth in their countries:

- 55 percent of respondents said IFRS adoption was "very important" to economic growth
- 35 percent said "important"
- 9 percent "somewhat important"
- 1 percent "not important"



In a survey conducted in late 2007 by the International Federation of Accountants (IFAC), a large majority of accounting leaders from around the world agreed that a single set of international standards is important for economic growth. Former AICPA Chairman Randy Fletchall, CPA, and AICPA President and CEO Barry Melancon, CPA, were among those surveyed. Of the 143 leaders from 91 countries who responded, 90 percent reported that a single set of international financial reporting standards was "very important" or "important" for economic growth in their countries (http://www.ifac.org/globalsurvey).

[1] Most EU countries currently do not permit use of IFRS in financial statements of privately held companies.

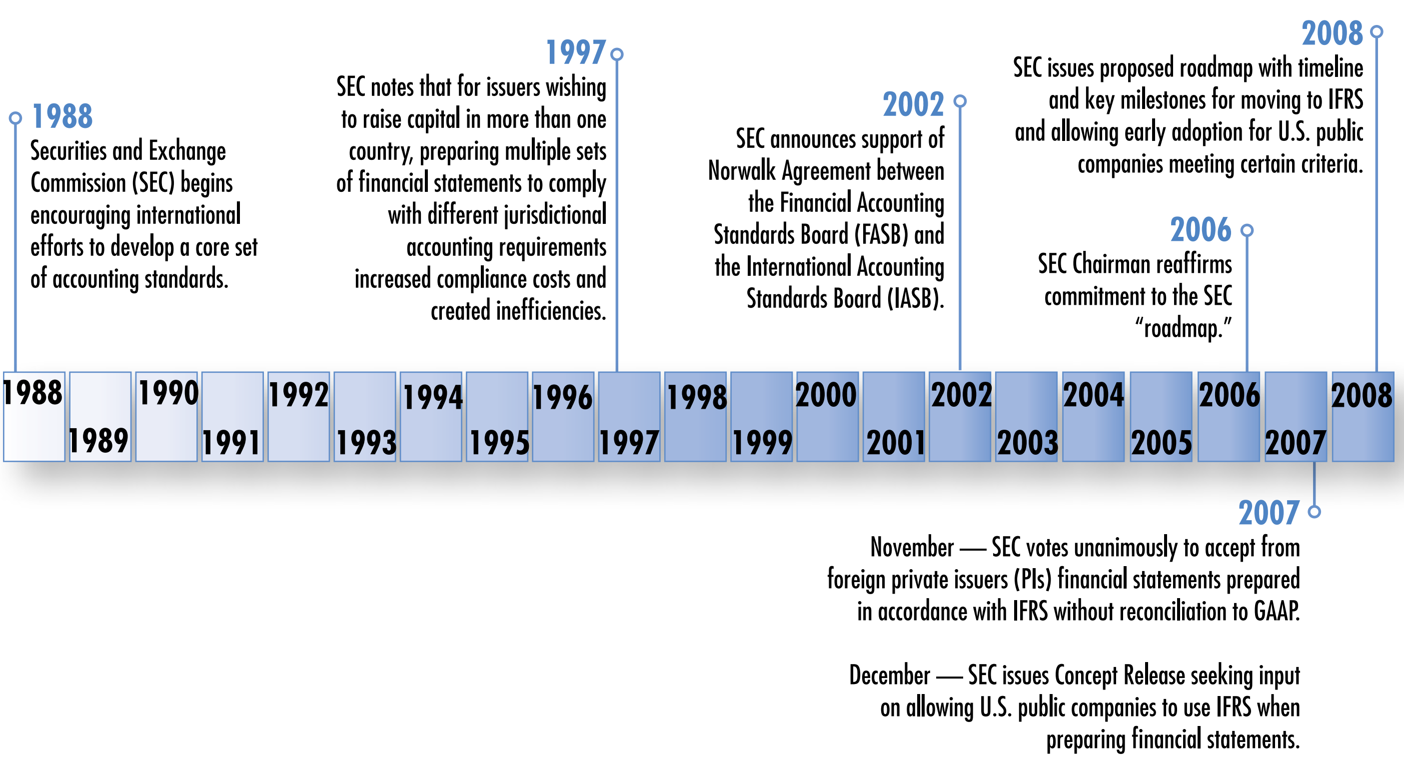
SEC Leadership In International Effort

The U.S. Securities and Exchange Commission has for many years been a strong leader in international efforts to develop a core set of accounting standards that could serve as a framework for financial reporting in cross-border offerings. It has repeatedly made the case that issuers wishing to raise capital in more than one country are faced with the increased compliance costs and inefficiencies of preparing multiple sets of financial statements to comply with different jurisdictional accounting requirements. In 2000, the International Organization of Securities Commissions (IOSCO), in which the SEC plays a leading role, recommended that its members allow multinational issuers to use 30 "core" standards issued by the IASB's predecessor body in cross-border offerings and listings.

A few years later, the SEC announced its support of a memorandum of understanding — the Norwalk Agreement — between the **Financial Accounting Standards Board (FASB)** and the International Accounting Standards Board. This agreement, concluded in Norwalk, Connecticut, established a joint commitment to develop compatible accounting standards that could be used for both domestic and cross-border financial reporting. In a subsequent memorandum of understanding, the FASB and the IASB agreed that a common set of high quality, global standards remained their long-term strategic priority and established a plan to align the financial reporting of U.S. issuers under U.S. GAAP with that of companies using IFRS.

Between 2005 and 2006, the number of foreign private issuers filing with the SEC using IFRS jumped from a handful to 110, and the SEC expects the number to continue to increase. In February 2006, SEC Chairman Christopher Cox reaffirmed the SEC's commitment to achieving one set of high quality, globally accepted accounting standards and opened the possibility that U.S. financial statements could be prepared using IFRS or U.S. GAAP.

SEC Timeline



In 2007, the SEC unanimously voted to allow foreign private issuers to file financial statements prepared in accordance with IFRS as issued by the IASB without reconciliation to GAAP. Of even greater importance was the SEC's Concept Release seeking input on allowing U.S. public companies to use IFRS when preparing financial statements. Most recently, the SEC issued a proposed **roadmap** that includes seven milestones for continuing U.S. progress toward acceptance of IFRS. The roadmap also would allow early adoption of IFRS for U.S. public companies that meet certain criteria.

Another recent development also points toward an accelerated convergence timeline. On September 11, 2008, the IASB and the FASB issued an update to their 2006 **memorandum of understanding** to state 2011 as the goal for completion of their major joint projects. The boards will work toward convergence of important accounting standards, such as revenue recognition, leases and consolidation. Resolution of differences in these key standards is a criterion for potentially moving U.S. public companies to IFRS. The FASB and the IASB say they will update the Norwalk Agreement to lay out a plan for one set of accounting standards from which all major capital markets would be able to operate by 2013. The boards will work to resolve differences believed to have impeded IFRS adoption in the U.S.

AICPA Participation

The AICPA was a charter member of the International Accounting Standards Committee (IASC), the IASB's predecessor organization. In the three decades since, the AICPA has worked to advance international convergence of accounting standards. Through its Accounting Standards Executive Committee (AcSEC), the AICPA provides thought leadership to the IASB on financial reporting topics. The Institute has made clear its support for giving U.S. issuers the option to prepare financial statements in accordance with IFRS as published by the IASB for purposes of complying with the rules and regulations of the SEC. The AICPA also is committed to supporting the nation's CPAs — largely financial statement preparers, auditors and educators — through an orderly transition.

Mindful of the importance of private companies and not-for-profit organizations, AICPA Council on May 18, 2008, voted to update Rule 203 of the Code of Professional Conduct to recognize the IASB as an international accounting standard setter. By removing a potential barrier, private companies and not-for profit organizations will have a clear option to decide if following IFRS makes sense for their situations and financial reporting constituents.

The AICPA understands that it will need to fulfill a number of responsibilities to make the use of IFRS by public companies a success. Ongoing efforts include:

- **Continuing to educate AICPA members about IFRS.**
- **Working with accounting educators, textbook authors and educational institutions to prepare future professionals to use IFRS.**
- **Making certain the voice of U.S. CPAs is heard internationally.**
- **Incorporating questions about IFRS into the Uniform CPA Exam.**

Two Sides Of The Story

Growing interest in the global acceptance of a single set of robust accounting standards comes from all participants in the capital markets. Many multinational companies and national regulators and users support it because they believe that the use of common standards in the preparation of public company financial statements will make it easier to compare the financial results of reporting entities from different countries. They believe it will help investors understand opportunities better. Large public companies with subsidiaries in multiple jurisdictions would be able to use one accounting language company-wide and present their financial statements in the same language as their competitors.

Another benefit some believe is that in a truly global economy, financial professionals including CPAs will be more mobile, and companies will more easily be able to respond to the human capital needs of their subsidiaries around the world.

Nevertheless, many people also believe that U.S. GAAP is the gold standard, and something will be lost with full acceptance of IFRS. However, recent SEC actions and global trends have increased awareness of the need to address possible adoption. According to a survey conducted in the first half of 2008 by Deloitte & Touche among chief financial officers and other financial professionals, U.S. companies have an interest in adopting IFRS and this interest is steadily growing. Thirty percent would consider adopting IFRS now, another 28 percent are unsure or do not have sufficient knowledge to decide, while 42 percent said they would not. Still, an AICPA survey conducted in Fall 2008 among its CPA members shows a significant and positive shift in the number of firms and companies that are starting to prepare for eventual adoption of IFRS. A 55 percent majority of CPAs at firms and companies nationwide said they are preparing in a variety of ways for IFRS adoption, an increase of 14 percentage points over the 41 percent who were preparing for change, according to an April 2008 AICPA survey.

Another concern is that worldwide, many countries that claim to be converging to international standards may never get to 100 percent compliance. Most reserve the right to carve out selectively or modify standards they do not consider in their national interest, an action that could lead to incomparability — the very issue that IFRS seek to address.

GAAP And IFRS, Still Differences

Great strides have been made by the FASB and the IASB to converge the content of IFRS and U.S. GAAP. The goal is that by the time the SEC allows or mandates the use of IFRS for U.S. publicly traded companies, most or all of the key differences will have been resolved.

Because of these ongoing convergence projects, the extent of the specific differences between IFRS and U.S. GAAP is shrinking. Yet significant differences do remain. For example:

- **IFRS does not permit Last In First Out (LIFO) as an inventory costing method.**
- **IFRS uses a single-step method for impairment write-downs rather than the two-step method used in U.S. GAAP, making write-downs more likely.**
- **IFRS has a different probability threshold and measurement objective for contingencies.**
- **IFRS does not permit curing debt covenant violations after year-end.**
- **IFRS guidance regarding revenue recognition is less extensive than GAAP and contains relatively little industry-specific instruction.**

Perhaps the greatest difference between IFRS and U.S. GAAP is that IFRS provides much less overall detail. As an example, IFRS fit into one book, about two inches thick, while the three FASB paperbacks of pronouncements plus the paperback version of the FASB Emerging Issues Task Force consensuses measure about nine inches thick, and that doesn't include all of the authoritative literature.

What CPAs Need To Know

The increasing acceptance of IFRS, both in the United States and around the world, means that now is the time to become knowledgeable about these changes. Most CPAs will somehow be affected. Once a critical mass of non-U.S. companies in a certain industry sector begin to report their financial results using IFRS, there will likely be pressure for U.S. issuers to do the same, to allow investors to better compare their financial results. But this issue will have an impact far beyond just financial reports. It will affect almost every aspect of a U.S. company's operations, everything from its information technology systems, to its tax reporting requirements, to the way it tracks stock-based compensation.

For the CPA profession, the use of IFRS by U.S. publicly held companies will create the need for effective training and education. Companies will use IFRS only if they and their auditors have been thoroughly trained, and if their investors and other users of their financial statements — such as analysts and rating agencies — understand IFRS as well. At the moment, most accountants in the United States are trained in U.S. GAAP, not IFRS. Most specialists, such as actuaries and valuation experts, who are engaged by management to assist in measuring certain assets and liabilities also are not taught IFRS. Consequently, all parties will need to undertake comprehensive training. Professional associations and industry groups will need to integrate IFRS into their training materials, publications, testing and certification programs. Colleges and universities will need to include IFRS in their curricula. If IFRS is accepted — and many think this is inevitable — as GAAP in the United States, it will be included in the Uniform CPA Examination.

The bottom line is that CPAs need to begin to prepare for the day in the not-so-distant future when the SEC could designate a date for voluntary, or even mandatory, adoption of IFRS by all U.S. public companies.

IFRS Conversion: Not Just an Accounting Exercise

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APPENDIX

Timeline for IFRS Acceptance in the United States

2001: The International Accounting Standards Board (IASB) is established as the successor organization to the International Accounting Standards Committee (IASC), formed in 1973. The IASB's mandate is to develop International Financial Reporting Standards (IFRS).

2002: The IASB and the Financial Accounting Standards Board (FASB) issue the Norwalk Agreement, acknowledging their joint commitment to developing high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. Also, the European Union (EU) announces that its member states will require IFRS in the preparation of consolidated financial statements of listed companies beginning in 2005.

2005: The chief accountant of the Securities and Exchange Commission (SEC) releases a roadmap allowing IFRS filings without GAAP reconciliation for foreign firms by 2009, or earlier.

2006: The IASB and the FASB agree to work on a number of major projects.

2007: The SEC announces that it will accept from foreign filers in the U.S. financial statements prepared in accordance with IFRS, as issued by the IASB, without reconciliation to U.S. GAAP. Also, the SEC issues a Concept Release asking if U.S. public companies should be given an option to follow IFRS instead of U.S. GAAP.

2008: The SEC issues a proposed roadmap that includes milestones for continuing U.S. progress toward acceptance of IFRS. The roadmap also would allow early adoption of IFRS for U.S. public companies that meet certain criteria. The AICPA's governing Council votes to recognize the IASB as an international accounting standard setter under rules 202 and 203 of the Code of Professional Conduct, thereby giving U.S. private companies and not-for-profit organizations a choice to follow IFRS. Also, the FASB and the IASB issue an updated Memorandum of Understanding that focuses the energies of both boards toward convergence of important accounting standards, such as revenue recognition, leases and consolidation.

2009: The IASB will end its moratorium, set in 2005, on the required application of new accounting standards and major amendments to existing standards. The board had frozen its rules while more countries adopted IFRS. Also, 2009 is the earliest year eligible early adopters could elect to use IFRS.

2011: Canadian and Indian companies are slated to begin using the global standards, and Japan is slated to have eliminated all major differences between Japanese GAAP and IFRS. SEC to evaluate feasibility of requiring use of IFRS based on achievement of key milestones in roadmap.

2012: Mexico scheduled to adopt IFRS for all listed entities. In the United States, questions concerning IFRS are expected to be included in the Uniform CPA Exam, if not sooner.

2014: Earliest year the SEC would require large accelerated filers to convert their financials to IFRS.

2015: Earliest year the SEC would require accelerated filers to convert their financials to IFRS.

2016: Earliest year non-accelerated filers, including smaller U.S. public companies, would be required to convert to IFRS.

2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2014-2016

2001
The International Accounting Standards Board (IASB) established.

2002
The IASB and the Financial Accounting Standards Board (FASB) issue the Norwalk Agreement.

The European Union (EU) announces member states must use IFRS beginning 2005 financial statements.

2005
Securities and Exchange Commission (SEC) releases a roadmap for allowing IFRS filings without GAAP reconciliation for foreign firms by 2009, or earlier.

2006
The IASB and the FASB agree to work on major projects jointly.

2007
The SEC announces foreign filers in the U.S. can file IFRS without reconciliation to U.S. GAAP.

SEC issues a Concept Release asking about U.S. public company option to follow IFRS instead of U.S. GAAP.

2008
The SEC issues proposed roadmap that includes milestones for continuing IFRS progress toward acceptance of IFRS. The FASB and the IASB issue an updated MoU focusing on convergence of key accounting standards by 2011.

The AICPA's governing Council votes to recognize IASB as an international accounting standard setter under the Code of Professional Conduct.

2009
The IASB will end moratorium on required application of new accounting standards and major amendments to existing standards.

2011
Canadian, Indian and Japanese companies are slated to begin using IFRS.

2012
Companies in Mexico scheduled to begin using IFRS.

2014-2016
Earliest years the SEC would require U.S. public companies to convert their financials to IFRS.

Organizations Involved

In April 2001, the **International Accounting Standards Board (IASB)**, an independent accounting standard-setter based in London, assumed accounting standard-setting responsibilities from its predecessor body, the International Accounting Standards Committee. The IASB is responsible for International Financial Reporting Standards (IFRS).

The **Securities and Exchange Commission (SEC)**, created in 1934 by an Act of Congress, is the U.S. government agency with primary responsibility for enforcing the federal securities laws and regulating the securities industry and the U.S. stock market. For the past three decades it has become increasingly vocal in its support of a single set of robust accounting standards that would be used worldwide.

The **American Institute of Certified Public Accountants (AICPA)**, with approximately 340,000 members, is the national professional organization for certified public accountants in the United States. Well before IFRS began to gain traction in the U.S. business and regulatory communities, the AICPA was publicly supporting the goal of a single set of high quality, global accounting standards to be used in the financial reporting of public companies throughout the world.

The **Financial Accounting Standards Board (FASB)** is working with the IASB to converge their respective accounting standards into a robust set of rules that will meet the needs of preparers and users worldwide.

The AICPA's **Accounting Standards Executive Committee (AcSEC)** is the senior technical committee of the AICPA authorized to speak on accounting matters. It provides accounting guidance to help financial professionals discharge their duties and serve the public interest.

For More Information:

American Institute of CPAs	www.aicpa.org
Financial Accounting Standards Board	www.fasb.org
International Accounting Standards Board	www.iasb.org
International Federation of Accountants	www.ifac.org
International Financial Reporting Standards Resources	www.ifrs.com
International Organization of Securities Commissions	www.iosco.org
Securities and Exchange Commission	www.sec.gov
SEC roadmap	www.sec.gov/spotlight/ifrsroadmap.htm

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