

International Financial Reporting Standards (IFRS)

An AICPA Backgrounder



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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. The number of countries that require or allow the use of IFRS for the preparation of financial statements by publicly held companies has continued to increase. In the United States, the Securities and Exchange Commission (SEC) is taking steps to determine whether to incorporate IFRS into the financial reporting system for U.S. issuers and, if so, when and how.

Worldwide Momentum

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.

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. Of the 143 leaders from 91 countries who responded, 90% reported that a single set of international financial reporting standards was “very important” or “important” for economic growth in their countries.

Currently, more than 120 nations and reporting jurisdictions permit or require IFRS for domestic listed companies. The European Union (EU) requires 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.² Brazil started using IFRS in 2010. Canada adopted IFRS, in full, on Jan. 1, 2011. Mexico will require adoption of IFRS for all listed entities starting in 2012. Japan is working to achieve convergence of IFRS and began permitting certain qualifying domestic companies to apply IFRS for fiscal years beginning April 1, 2010. A decision regarding the mandatory use of IFRS in Japan is to be made around 2012. Hong Kong has adopted national standards that are equivalent to IFRS and China is converging its accounting standards with IFRS. Other countries have plans to adopt IFRS or converge their national standards with IFRS.

In addition to the support received from certain U.S.-based entities, financial and economic leaders from various organizations have announced their support for global accounting standards. Leaders of the Group of 20 (G20) called for global accounting standards and urged the U.S. Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) to complete their convergence projects in 2011. A summary of the IASB and FASB's efforts regarding convergence is subsequently described.

SEC Leadership in International Effort

The 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 FASB and the IASB. This agreement, concluded in Norwalk, CT, 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 in September 2008, 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. generally accepted accounting principles (GAAP) with that of companies using IFRS.

¹ The European Union (EU) has adopted virtually all International Financial Reporting Standards (IFRSs), though there is a time lag in adopting several recent IFRSs. In the EU, the audit report and basis of presentation note refer to compliance with "IFRSs as adopted by the EU."

² Israel requires IFRS for all companies, except banks and companies dually listed in the U.S. and Israel. Dually listed companies have the option to use IFRS or U.S. GAAP. Australia and New Zealand have adopted national standards that they describe as IFRS-equivalents.

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 U.S. 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. In November 2008, the SEC issued a proposed roadmap that included seven milestones for continuing U.S. progress toward acceptance of IFRS. The roadmap generated significant interest and thoughtful comments from investors, issuers, accounting firms, regulators and others regarding factors the SEC should consider.

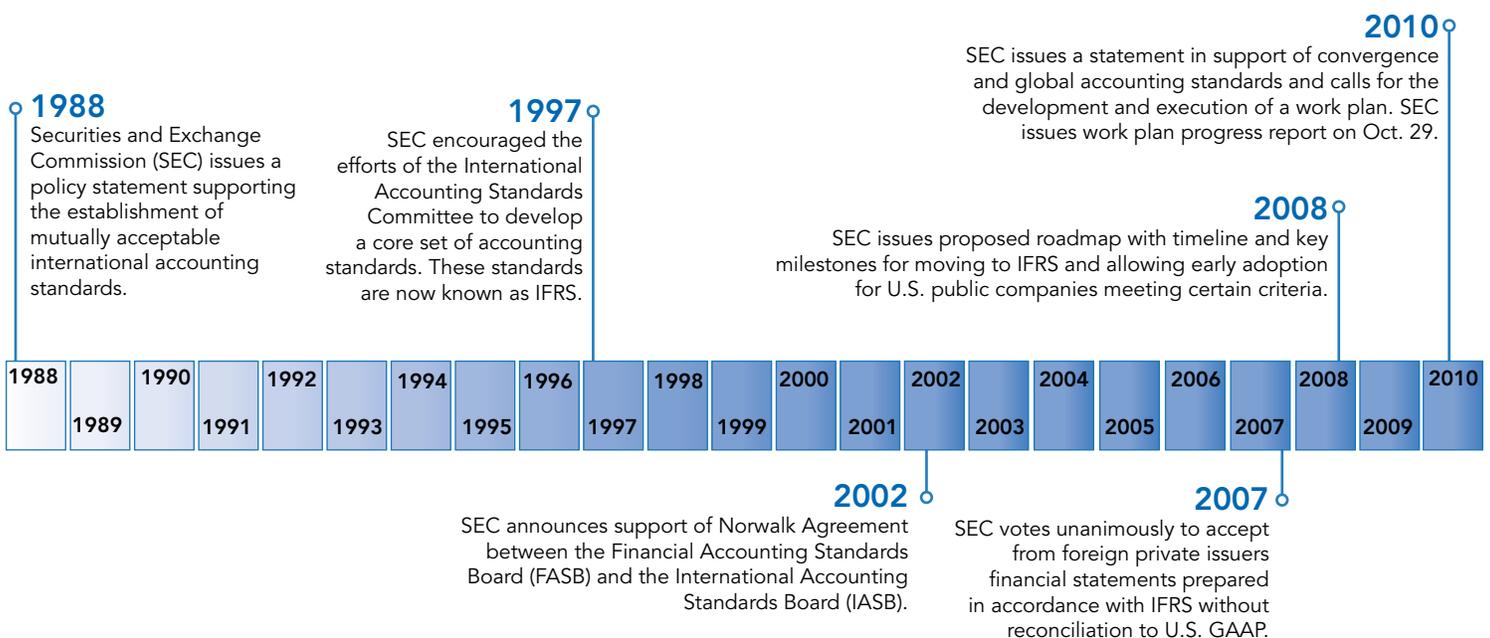
On Feb. 24, 2010, the SEC issued Release Nos. 33-9109 and 34-61578, Commission Statement in Support of Convergence and Global Accounting Standards, in which the SEC stated its continued belief that a

single set of high-quality globally accepted accounting standards would benefit U.S. investors and expressed encouragement for the continued convergence of U.S. GAAP and IFRS. The releases also called for the development and execution of a "work plan" to enhance both the understanding of the SEC's purpose and public transparency in regard to IFRS. The work plan addresses many of the areas of concern highlighted in the comment letters to the 2008 roadmap.

The SEC Work Plan

The work plan includes consideration of IFRS, both as they currently exist and after the completion of the various convergence projects under way by the FASB and the IASB. Among other things, the work plan addresses some of the comments and concerns received in response to the SEC's proposed roadmap issued in November 2008, including the following:

SEC Timeline



- Determining whether IFRS is **sufficiently developed and consistent** in application for use as the single set of accounting standards in the U.S. reporting system
- Ensuring that accounting standards are set by an **independent standard setter** and for the benefit of investors
- **Investor** understanding and **education** regarding IFRS and how it differs from U.S. GAAP
- Understanding whether **U.S. laws or regulations**, outside of the securities laws and regulatory reporting, would be affected by a change in accounting standards
- **Understanding the impact on companies** both large and small, including changes to accounting systems, changes to contractual arrangements, corporate governance considerations and litigation contingencies
- Human capital readiness – determining whether the people who prepare and audit financial statements are sufficiently prepared, through education and experience, to convert to IFRS

On Oct. 29, 2010, the SEC released a progress report on its IFRS Work Plan. The report provided details on progress and remaining research and analysis to be done as the SEC considers whether to incorporate IFRS into the U.S. financial reporting system for U.S. issuers.

In 2011, assuming completion of the convergence projects and the SEC staff's work plan, the SEC will decide whether to incorporate IFRS into the U.S. financial reporting system for U.S. issuers, and if

so, when and how. If the SEC determines to incorporate IFRS into the U.S. financial reporting system, the SEC believes the first time U.S. entities would be required to report under such a system would be no earlier than 2015. This timeline will be further evaluated as part of the work plan. The work plan is included as an appendix at the end of the SEC's release, which is located on the SEC's website at the following address: sec.gov/rules/other/2010/33-9109.pdf.

Additional information, including the SEC's progress report, can be found at the following address: sec.gov/spotlight/globalaccountingstandards.shtml.

FASB and IASB Convergence Efforts

The FASB and the IASB have been working together toward convergence since 2002. The two boards have described what convergence means and their tactics to achieve it in two documents — the Norwalk Agreement issued in 2002 and the Memorandum of Understanding (MoU), originally issued in 2006 and updated in 2008. The MoU originally highlighted several major convergence projects between IASB and FASB scheduled for completion in 2011. In response to the requests from the leaders of the G20, the IASB and FASB published a progress report, describing an intensification of their work program, including monthly joint board meetings and quarterly progress updates on these convergence projects.

On Nov. 29, 2010, FASB and IASB issued a convergence progress report. In the report, the standard setters reaffirmed their priority projects for completion by June 30, 2011, or earlier. Joint priority projects include financial instruments,



revenue recognition, leases, presentation of other comprehensive income and fair value measurement. For the IASB, projects scheduled for completion by the end of June 2011 include improved disclosures about derecognized assets and other off-balance sheet risks, consolidations and its project on insurance contracts.

The boards decided to defer until after June 2011 substantive deliberations on four projects including the broader financial statement presentation project, financial instruments with characteristics of equity, emissions trading schemes and the reporting entity phase of the conceptual framework. The boards also agreed that consolidation of investment companies is no longer a priority for June 2011.

The FASB and IASB also deferred deliberations on several of their independent standard-setting projects (such as contingency disclosures for

the FASB and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and annual improvements for the IASB).

Of the remaining original projects in the 2006 MoU, Business Combinations has been completed. Intangible Assets has been removed from the active agendas of both boards and Post-Employment Benefits was removed from the list of priority MoU projects in October 2009.

For more information on convergence, visit the [Convergence Section](#) of IFRS.com.

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.

The AICPA provides thought leadership to the IASB on financial reporting topics. The Institute has made clear its support for the goal of a single set of high-quality, global accounting standards to be used by public companies in the preparation of transparent and comparable financial reports throughout the world and believes the standards issued by the IASB are best positioned to become those standards. In response to the SEC's endorsement of a work plan, as previously mentioned, Barry Melancon, AICPA President and Chief Executive Officer, reiterated the AICPA's continued support of the "thoughtful and concrete steps the SEC is taking" to prepare for the possible transition to IFRS. 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 recognize the IASB as an international accounting standard setter under Rules 202 and 203 of the Code of Professional Conduct. Appendix A to Rules 202 and 203 of the AICPA's Code of Ethics sets forth the standard setters that have been designated by the Council. Under Rule 202, a member who performs professional services shall comply with the standards promulgated by the designated bodies. Additionally,

a member may not say that financial statements are in accordance with generally accepted accounting principles unless they follow the standards promulgated by a standard setter listed in Appendix A of Rule 203. By removing a potential barrier, private companies and not-for-profit organizations have a clear option to decide if following IFRS makes sense for their situations and financial reporting constituents.

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. Recent SEC actions and global trends have increased awareness of the need to address possible adoption.

The AICPA conducts a semi-annual IFRS Readiness Survey. In its fall 2010 survey, 54% of respondents said that the SEC should ultimately require adoption of IFRS for U.S. public companies, although most believe more convergence of accounting standards is needed first. Another 21% said IFRS should be available as an option for use by U.S. public companies. A survey of more than 2,500 executives by global accounting firm KPMG, taken subsequent to the SEC's February 2010 Work Plan release, found that 49% of U.S. executives want the option to move to IFRS earlier than the SEC 2015 potential adoption date, if the SEC makes a decision in 2011 to allow IFRS for U.S. issuers. Nevertheless, many people also believe that U.S. GAAP is the gold standard, and some degree of quality will be lost with full acceptance of IFRS. Another concern is that worldwide, many countries that claim to be converging to international standards may never get to 100% 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.

Differences Remain Between U.S. GAAP and IFRS

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, many 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 allows the revaluation of assets in certain circumstances.
- 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 requires capitalization of development costs, when certain criteria are met.

Perhaps the greatest difference between IFRS and U.S. GAAP is that IFRS provides less overall detail and industry-specific guidance.

What CPAs Need To Know

The increasing acceptance of IFRS, both in the U.S. 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 begins 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 experienced with 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 are including IFRS in their curricula. In addition, the Uniform CPA Exam now contains questions related to IFRS.

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.

The AICPA understands 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

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 the 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 U.S. 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 the 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 ended 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. Japan introduces a roadmap that could lead to a decision in 2012 to adopt IFRS, with proposed adoption dates in 2015 or 2016.

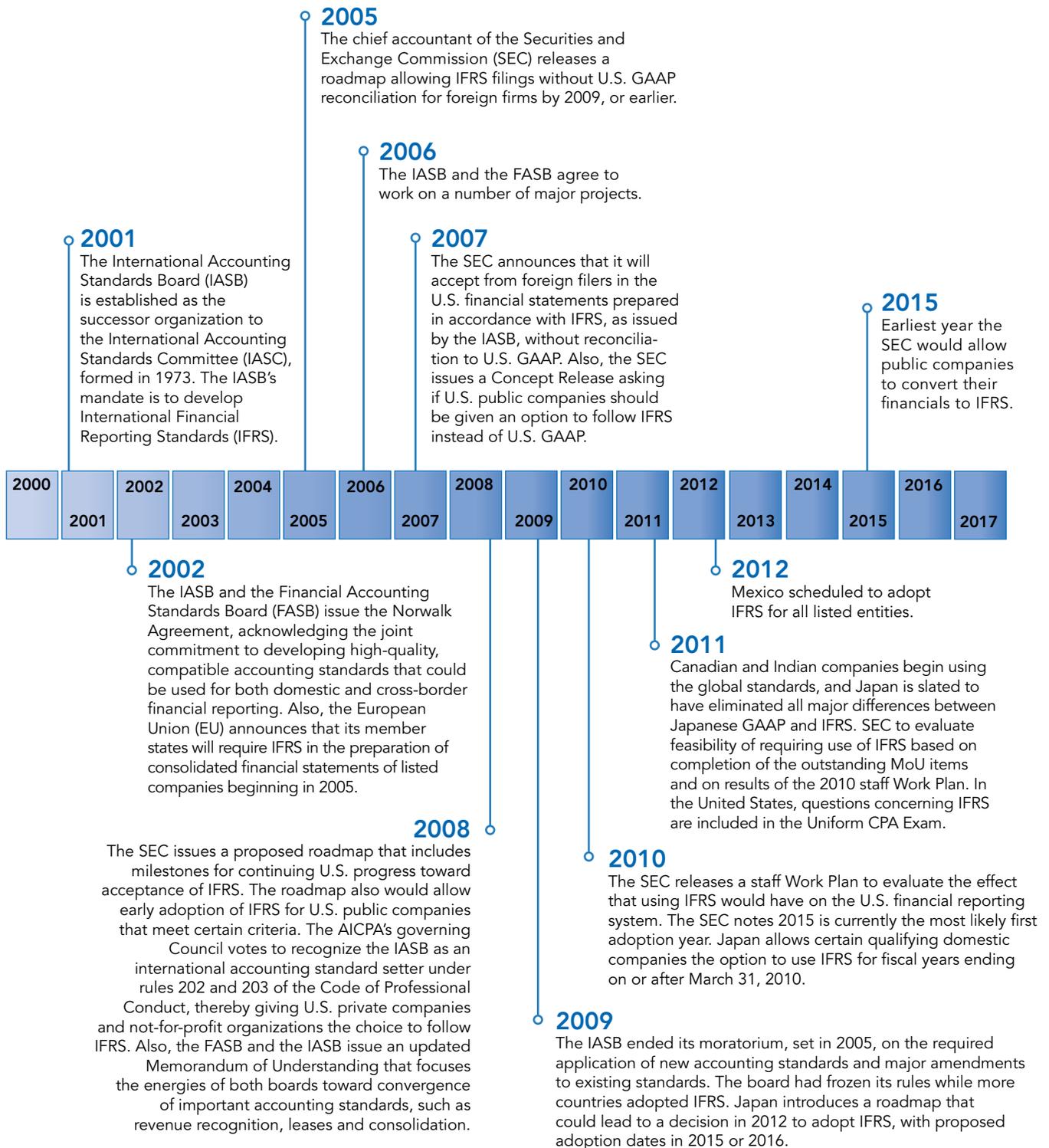
2010: The SEC releases a staff Work Plan to evaluate the effect that using IFRS would have on the U.S. financial reporting system. The SEC notes 2015 is currently the most likely first adoption year. Japan allows certain qualifying domestic companies the option to use IFRS for fiscal years ending on or after March 31, 2010.

2011: Canadian and Indian companies 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 completion of the outstanding MoU items and on results of the 2010 staff Work Plan. In the United States, questions concerning IFRS are included in the Uniform CPA Exam.

2012: Mexico scheduled to adopt IFRS for all listed entities.

2015: Earliest year the SEC would allow public companies to convert their financials to IFRS.

IFRS Timeline



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) is the world's largest organization representing the accounting profession, with nearly 370,000 members in 128 countries. 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 Financial Reporting Executive Committee (FinREC) 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	aicpa.org
Financial Accounting Standards Board	fasb.org
International Accounting Standards Board	iasb.org
International Federation of Accountants	ifac.org
AICPA IFRS Resources	ifrs.com
International Organization of Securities Commissions	iosco.org
Securities and Exchange Commission	sec.gov/spotlight/globalaccountingstandards.shtml
SEC Release Nos. 33-9109 and 34-61578	sec.gov/rules/other/2010/33-9109.pdf

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