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Implications of EU adoption of IFRS for practice.

AAA IAS Luncheon
San Francisco, 8 August 2005

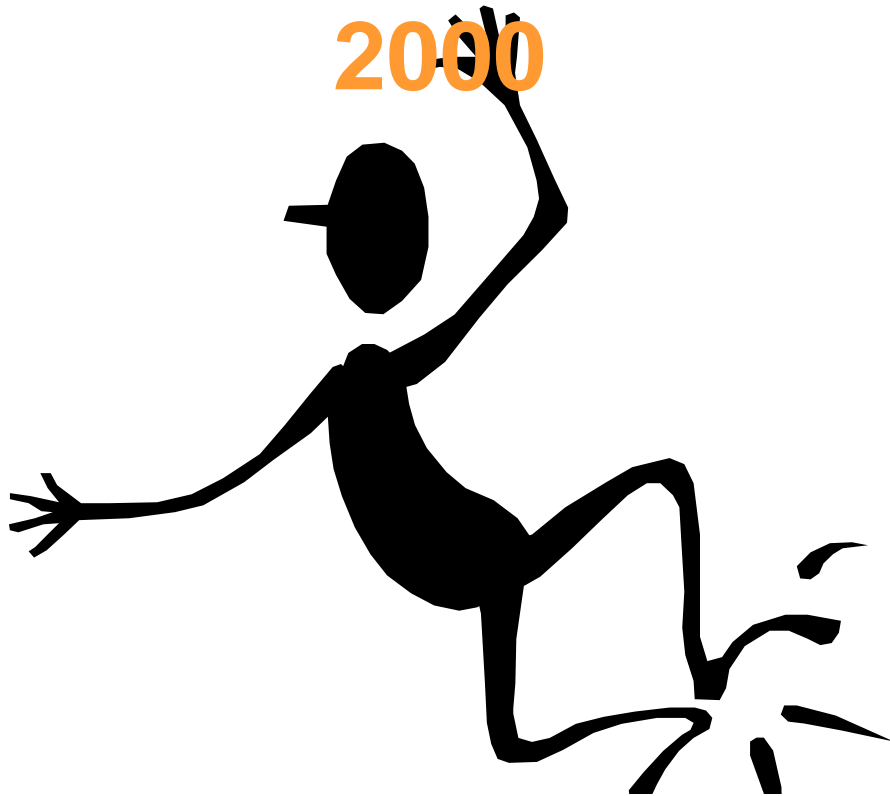
Andreas Barckow
National IFRS Experts Leader, Germany.

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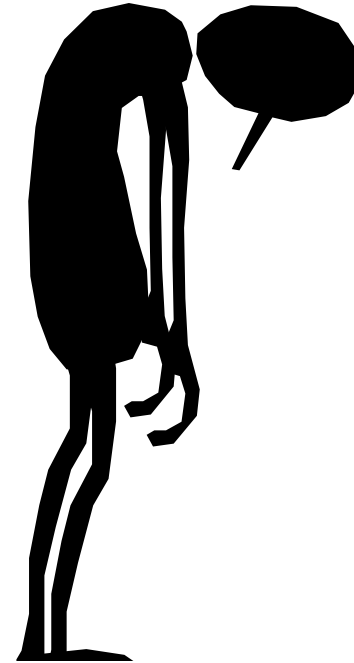
Audit . Tax . Consulting . Corporate Finance .



IFRS in Europe 2000



IFRS in Europe 2005



Is the party over?

- ▶ The legal framework: the EU Commission's IAS Regulation
- ▶ Issues frequently seen on conversions
- ▶ Possible issues for future research

1978: 4th Directive (Individual Accounts)



1983: 7th Directive (Consolidated Accounts)

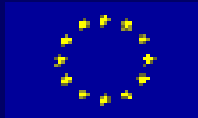
1995: EU Commission agrees on new accounting strategy (follow IAS instead of developing the directives further)

2000: Commission announces plan to require IAS for group accounts of listed companies by 2005

2001: *Fair Value Directive* (require/allow for fair value measurement of certain financial instr.)

2002: *IAS Regulation* (listed groups must follow IAS)

2003: *Modernization Directive* (enhance financial reporting by "brushing up" directives → IFRS)



	Individual accounts	Group accounts
Companies <u>with listed securities</u>	member state option	IFRS mandatory from 2005/7
Companies <u>with no listed securities</u>	member state option	member state option



Individual accounts

Group accounts

Companies
with listed
securities

- German GAAP accounts still mandatory!

IFRS
mandatory
from 2005/7

Companies
with no listed
securities

- May file IFRS accounts with the Federal Register

company
option

* For a full list of member states' implementation go to <http://www.iasplus.com>

ESBG

EFFAS

EFB

EFAA

CEA

FEE

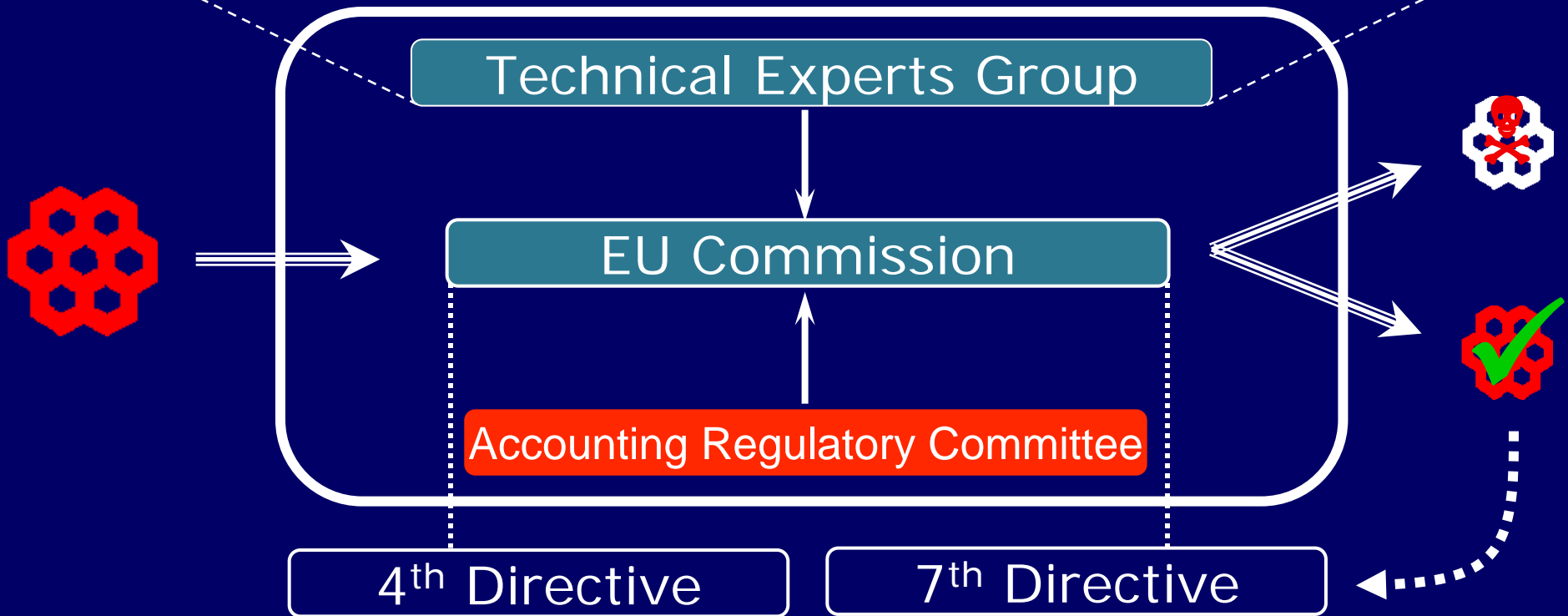
FESE

GEBC

UNICE

UEAPME

European Financial Reporting Advisory Group (EFRAG)



▶ **Regulation overload**

- too many changes occurring at about the same time (FSAP: IFRS, Basle II, Prospectus Directive ...)

▶ **Failure to realize the degree of change on FTA**

- technical differences to local GAAP
- timing: conversion could last up to 24 months
- necessary system changes/enhancements

▶ **Shortage of well-trained personnel**

▶ **Perceived lack of influence on the IASB**

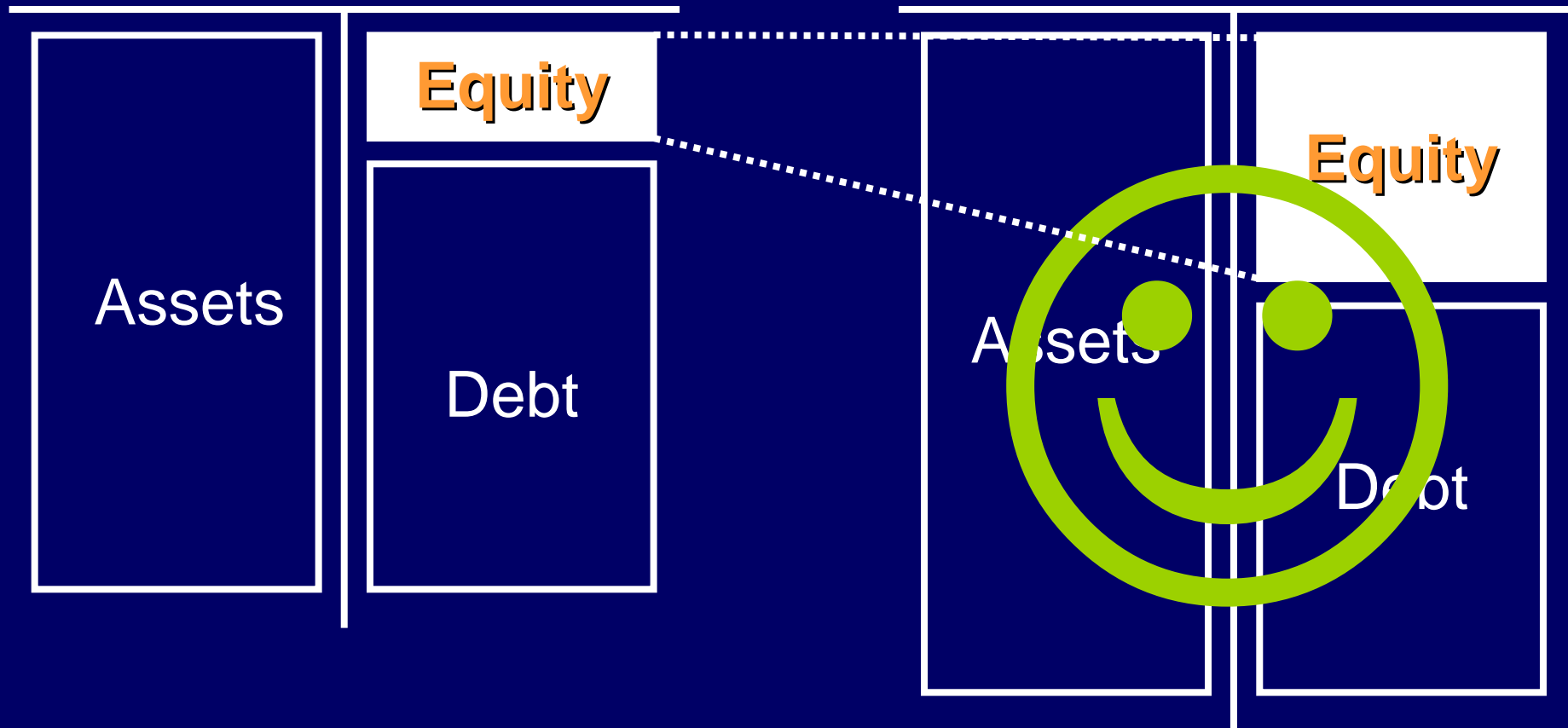
“they do neither understand nor listen ...”

Some widely expected implications of an IFRS conversion on P&L and equity

	P&L	Equity
Capitalization of Development Cost	↑	↑
Non-Amortization of Goodwill	↑	↑
Change of Depreciation Methods	↑	↑
Reclassification of Leases	—	—
Fair Value Measurement of Securities and Derivatives	↑↓	↑↓
Change in Measuring Inventory	↑	↑
Change in Recognition of Provisions	↑	↑
Increase in Pension Liabilities	↓	↓
Comprehensive Recognition of Deferred Taxes	↑↓	↑↓
Consolidation of SPEs	↑↓	—

local GAAP

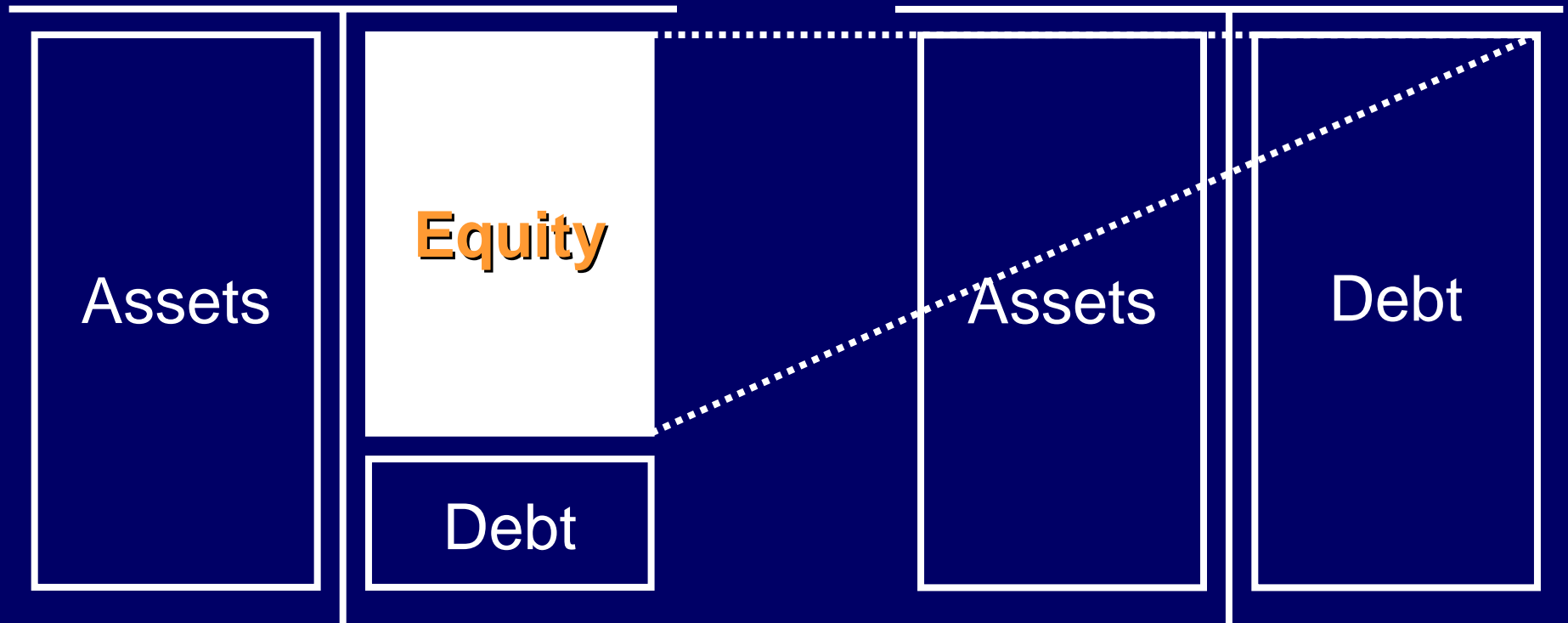
IFRS



Assume, company is partnership / coop / mutual entity

local GAAP

IFRS



▶ IAS 12

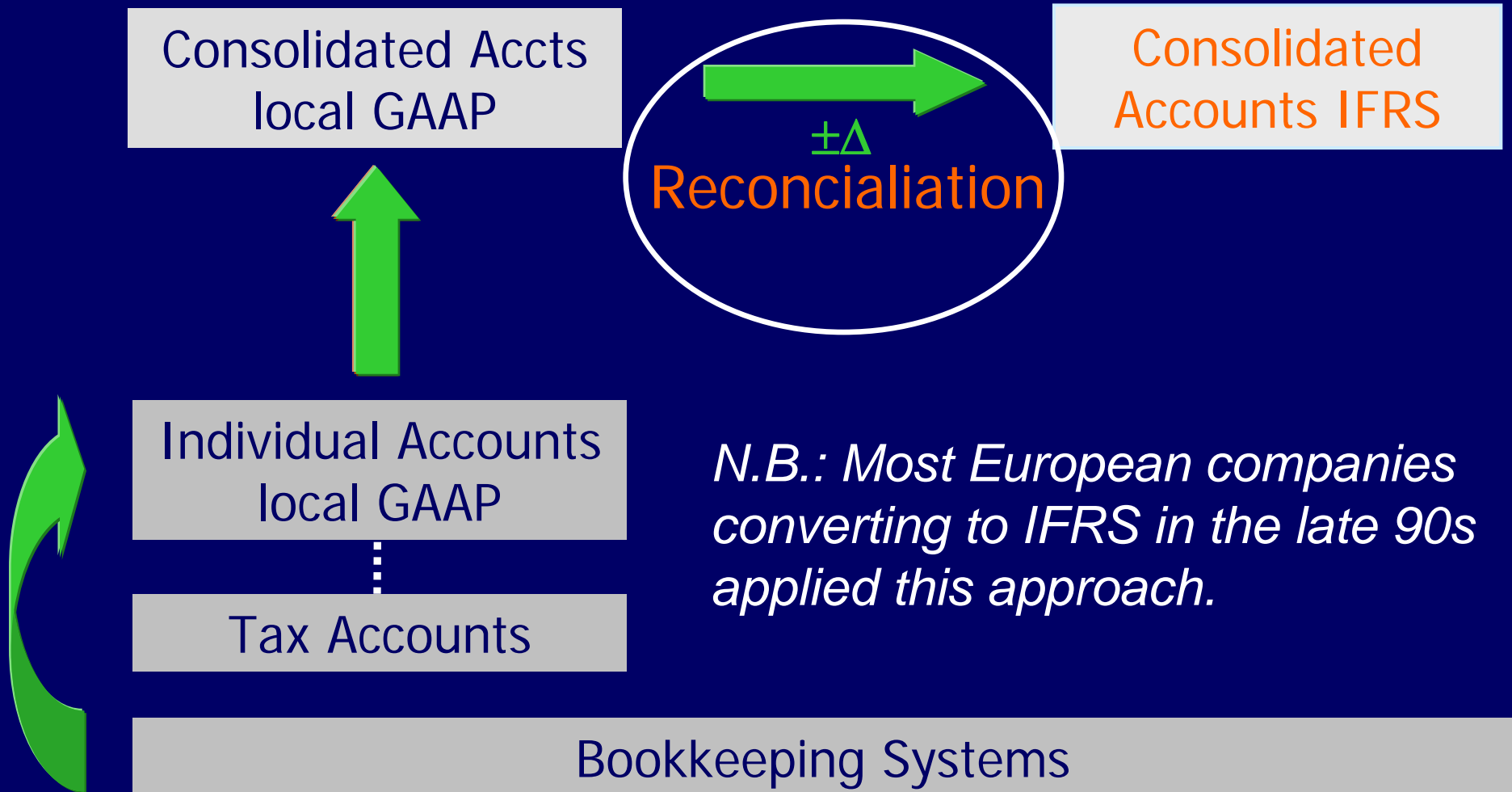
- Temporary differences approach

▶ IAS 32/39

- Debt/Equity → mandatorily redeemable capital
- Derivatives → detection of embedded derivatives, measurement
- Derecognition → many securitizations fail
- Impairment → loan loss provisioning
- Hedge Accounting → macro “hedging” strategies

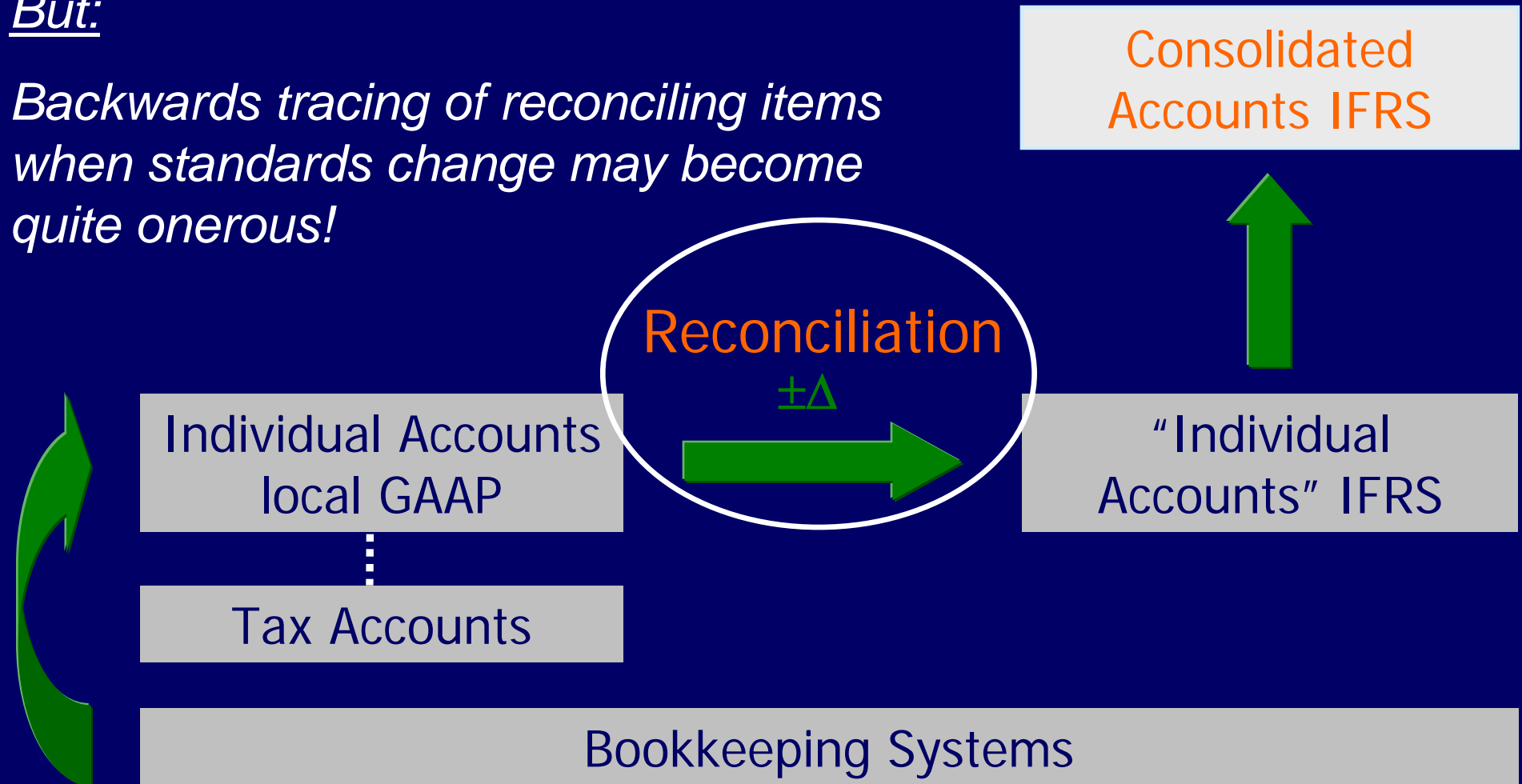
▶ IFRS 3

- Impairment Test



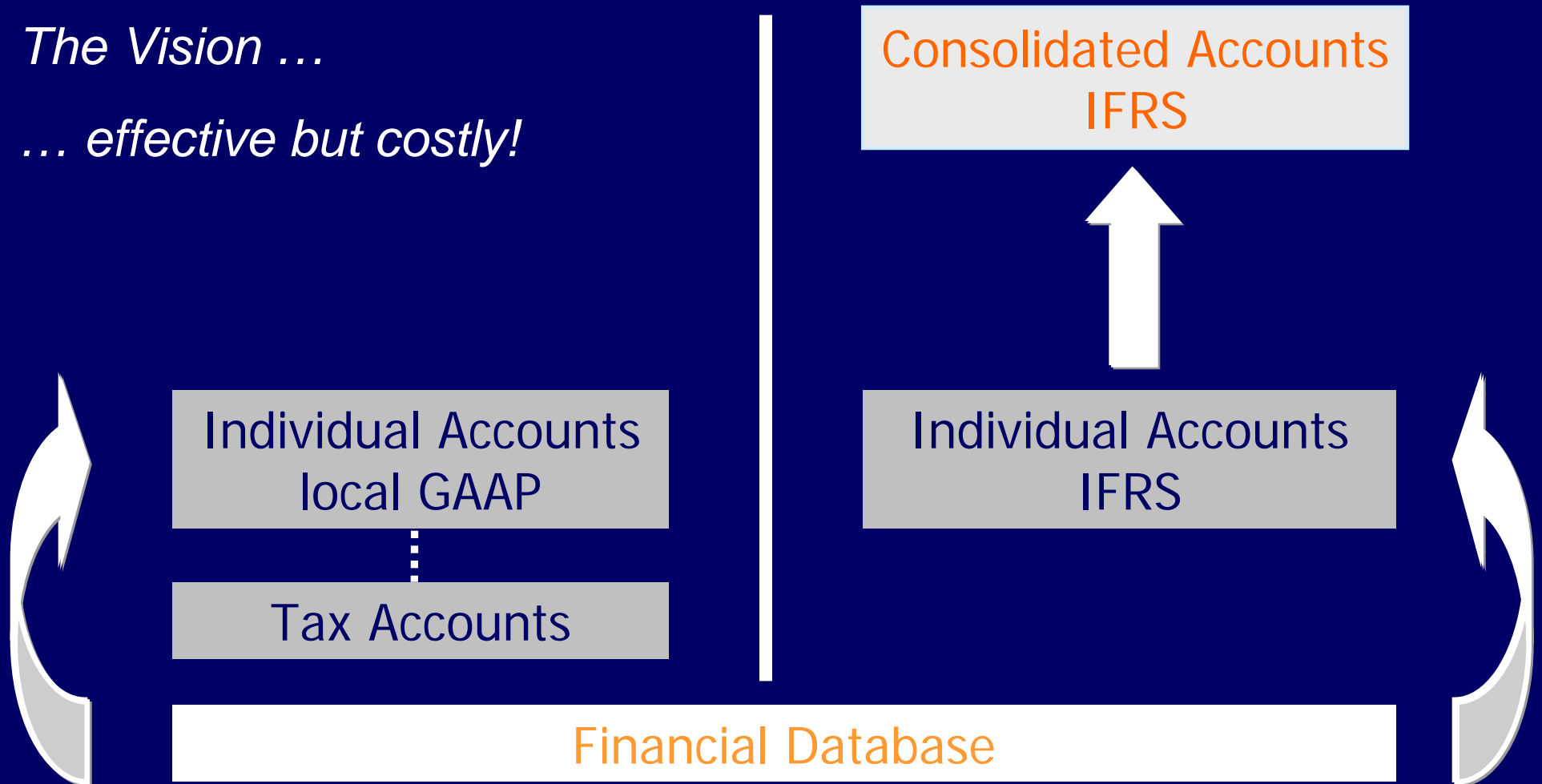
But:

Backwards tracing of reconciling items when standards change may become quite onerous!



The Vision ...

... effective but costly!



- ▶ Does/did mandatory implementation of IFRS in Europe
 - ▶ enhance comparability of accounts?
 - ▶ decrease stock market volatility?
 - ▶ lead to lower cost of capital?
(all as compared to previous GAAP)
- ▶ Is there (still) a preference for IFRS accounts over local GAAP accounts
 - ▶ across users of financial statements?
 - ▶ across Europe?
- ▶ Impact on enforcement? convergence? ...?

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