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IFRS Newsletter for U.S. Companies

IFRS: Latest Developments

The SEC extends the comment period for the proposed IFRS roadmap…
Incoming SEC Chairperson Mary Schapiro comments on IFRS…
The newly formed Financial Crisis Advisory Group meets to address accounting and the global financial credit crisis...

News reports about recent IFRS activity have been abundant. With a new administration and the ongoing financial crisis, debate around IFRS continues, including the need for a single set of global accounting standards and the pace of acceptance of IFRS in the U.S. To help executives keep track of the latest developments and to provide perspective on recent changes, a brief overview of key events follows.

Comment Deadline

The Securities and Exchange Commission (SEC) has extended the comment period for its proposed IFRS roadmap. Originally February 19, 2009, the comment deadline was extended to April 20, 2009 in response to requests received by the SEC that indicated additional time would improve the potential response rate and quality of responses.

The proposed roadmap sets forth milestones that, if achieved, could lead to the required use of IFRS for U.S. issuers beginning in 2014. The IFRS roadmap also contains proposed rule changes that would give certain U.S. issuers the option to use IFRS earlier, beginning in 2009.

Many comments received to date acknowledge the importance of the SEC's efforts to develop high-quality standards that improve transparency and the usefulness of financial reporting. Initial comment letters have also raised the following issues: the status of convergence between FASB and IASB; perceived demand from investors for IFRS; the cost of conversion in a challenging economic environment; and appropriate regulatory oversight of the standard-setting process.[1]

continued on next page

[1] Securities and Exchange Commission website: http://www.sec.gov/comments/s7-27-08/s72708.shtml.

IFRS: Latest Developments (continued)

New SEC Chairperson

Mary Schapiro, the new SEC Chairperson confirmed in January, has provided preliminary commentary on IFRS indicating a need for further study of IFRS, including issues regarding the independence of the IASB, costs of IFRS conversion, and the absence of industry guidance under IFRS. However, Ms. Schapiro has confirmed her broad support for global standards: "I think we all can agree that a single set of accounting standards used around the world would be a very beneficial thing [that] would allow investors to compare companies around the world."[2]

With the backdrop of administration changes, Paul Volcker, Chairman of the Economic Recovery Advisory Board has stated support for IFRS: "I do think we ought to be working toward international accounting standards and have them standard around the world under the general aegis of the International Accounting Standards Board, and there's been a lot of progress in that direction."[3]

The Financial Crisis Advisory Group Meets[4]

The Financial Crisis Advisory Group (FCAG) — established by both the International Accounting Standards Board (IASB) and the U.S. Financial Accounting Standards Board (FASB) — was formed to address the role of financial reporting amid the global financial crisis and identify key issues for rule makers to focus on over the next year. The first meeting was held in London on January 20, 2009; and the second was on February13, 2009 in New York.

At the January meeting, two main questions framed the day's discussion: "Where did financial reporting help identify issues during the crisis?" and "Where did financial reporting not help?" Chairman of the FASB, Robert Herz, and Chairman of the IASB, Sir David Tweedie, provided updates on actions taken by both boards and acknowledged growing pressure for more fundamental changes to financial reporting.

They outlined five major issues that emerged during the crisis: 1) fair value; 2) off-balance sheet activities (consolidation); 3) securitization (derecognition); 4) impairment; and 5) risk reporting. The chairmen elaborated on actions taken and planned to address those issues. Staff from both boards gave detailed updates as well.

Providing a summary of a recently published SEC report on the impact of fair value accounting on the financial crisis in the U.S., James Kroeker, SEC Acting Chief Accountant, noted that the majority of assets in financial statements of U.S. financial institutions were not measured at fair value — and only a fraction of those were measured with changes in fair value being recorded in the profit and loss statement. The report concluded that fair value did not play a meaningful role in the crisis; and noted that fair value was considered useful by investors.

FCAG members expressed their views — with main themes summarized below.

Fair value — Although some participants expressed the view that fair value played a role during the financial crisis, the majority indicated fair value did not play a major role and none of the participants proposed to abandon it. The business risks that financial institutions took on and did not appropriately manage was a point emphasized. It was highlighted that entities would need more guidance on how to determine fair value under specific circumstances, particularly in inactive markets. Other FCAG members were concerned that the valuation process itself was not transparent and that this needed to be addressed.

Many FCAG members highlighted that off-balance sheet activities and consolidation rules allowed the development of a shadow accounting system where risks were not presented in any financial statement. It was noted that management needs to explain in its financial reports why entities are consolidated or not.

Due process in standard setting — Many participants emphasized the importance of adhering to due process, even in situations where accelerated solutions were sought. It was noted that shortcuts to due process could undermine investors' confidence in financial reporting. Some members stressed the need for a single global set of standards.

Investor confidence — Some participants emphasized the importance of investor confidence in financial reporting and its role in improving market conditions.

Impairment — Many FCAG members were concerned over the complex rules on impairment and the differences between IFRS and U.S. GAAP.

As global competitors embrace the standards, more U.S. companies are recognizing the need to keep current on IFRS and consider the lessons learned from Europe and other countries that have converted to IFRS. Making an initial and low investment in IFRS early on — to gain headway on the timeline — could help U.S. companies avoid costly surprises later.

2 The U.S. Senate Committee on Banking, Housing, and Urban Affairs hearing on the nomination of Mary L Schapiro as Chairman of the Securities and Exchange Commission, 15 January 2009. Click here for the Webcast of the Hearing.

3 CFO.com, "Top Obama Advisers Clash on Global Accounting Standards," January 16, 2009.

4 This summary is adapted from IASPlus.com notes, which were taken by observers at the FCAG meeting, and should not be regarded as an official or final summary.

Making It Happen: IFRS and Human Resource Issues

IFRS transition activities are not limited to the realm of accounting and financial reporting. Leaders from around the entire organization have a role to play in contributing to the company's IFRS plan and strategy. This includes the chief human resource officer (CHROs) who can help address the central planning question, "How can we best prepare the organization — and the employees — for IFRS changes?" Human resource (HR) issues — such as enterprise-wide training, qualified personnel, communications, and process updates — are key factors in developing the overall conversion plan.

Outlined here are a few HR considerations for c-suite leaders in charge of their IFRS initiative.

Organizational structure and roles — Identify current IFRS reporting obligations for statutory or other purposes and assess how the organization is addressing these. Review potential risks in evaluating the existing processes, governance, and reporting structures. Consider the benefits of an IFRS shared service center to help centralize and streamline financial reporting processes.

Skills and capabilities — Assess IFRS capabilities and skills throughout the organization and identify existing resources. Define knowledge and capability gaps to determine training requirements and appropriate training delivery methods. Identify how to leverage a global IFRS talent pool. Determine how training can be aligned with existing compliance and regulatory programs.

Compensation and rewards — From a technical perspective, the accounting for many compensation programs (such as pension, postretirement medical and share-based payments) is significantly different under IFRS compared to U.S. GAAP. These program designs will need to be reviewed and possibly modified.

Five HR-Related Questions

1. Do my finance, accounting, and corporate officers have access to IFRS analysis that will inform our assessment activities, conversion roadmap, and overall IFRS strategy?
2. Are my organization's HR and rewards structures designed to support IFRS conversion activities?
3. Do I understand the impact of IFRS on key employees' roles and responsibilities?
4. Have I positioned my organization for success with the right program management and governance structure to see the IFRS assessment and conversion through a multi-year process?
5. Does my team, or my IFRS conversion advisory partner, have the capabilities and resources to meet the challenges of a successful IFRS conversion reflecting not only technical accounting implications, but also the broader HR aspects?

Communications — Identify key stakeholders — who align leadership and management — to deliver messages regarding the conversion plan and interim steps. Make sure the finance and accounting functions have support in communicating IFRS-related changes to the business. Enable open communication between subsidiaries and the parent company. Customize communications for the right audience — some messages may need to relay detailed technical guidance, while others may be more process-oriented. Identify communication channels (e.g. intranet and email distributions) to share knowledge across the organization. In addition, consider developing an external communication strategy to educate and inform investors, analysts, and shareholders.

Evaluating these human resource issues related to an IFRS conversion can help bolster the IFRS conversion plan. Incorporating these elements into the IFRS strategy early can help save time, effort, and resources over the long term.

Coming soon: Deloitte Consulting LLP publication, "Addressing the complexity of IFRS: Considerations for the people-related challenges of conversion."

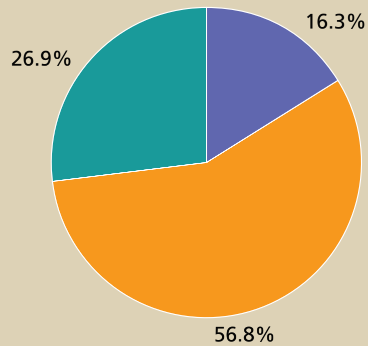
New: IFRS Considerations for Audit Committees

This new publication is designed to assist audit committee members in preparing for meaningful and effective conversations about IFRS. Access the publication to learn more.

A View From The Field: Private Companies & IFRS

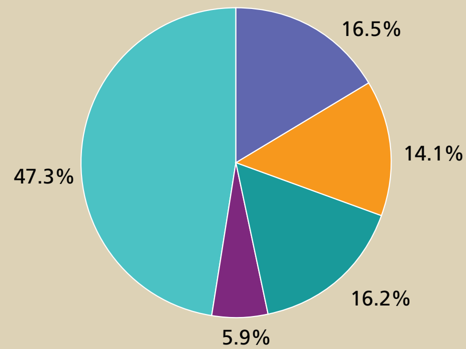
The International Accounting Standards Board (IASB) is expected to complete its project on IFRS for Private Entities (IFRS-NPAEs) in 2009. This tailored version of full IFRS could be very appealing for private companies. According to a recent Deloitte webcast poll,[5] more than 40 percent of finance professionals said their companies would take positive action when the IASB completed its project on private company reporting, clearly showing a strong interest in IFRS. Results include:

Are you aware of the IASB's project on IFRS-NPAEs?



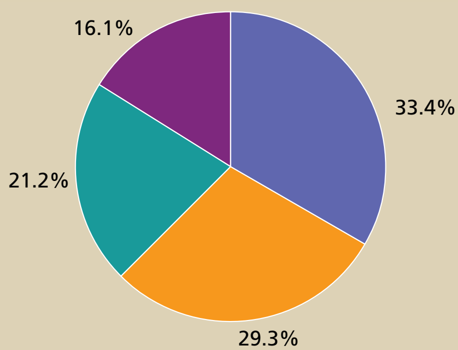
- Yes, I've been following the project
- Somewhat, I've heard of it, but haven't been following in detail
- No, I'm not aware any such development is taking place

IFRS-NPAEs would be an attractive opportunity to our company, if the accounting for income taxes is based on the:



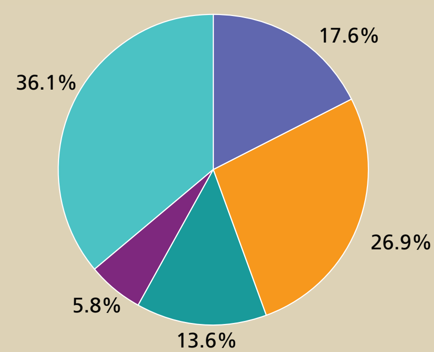
- Taxes payable approach
- Asset/liability approach including the accounting for deferred taxes
- Accounting for income taxes would not be a factor in our decision to adopt IFRS – NPAEs
- We prefer to issue a financial statements on the income tax basis of accounting
- Don't know/not applicable

What aspects of IFRS-NPAEs do you find most attractive?



- Simplified, self-contained set of accounting standards that are appropriate for NPAEs
- Reduced financial reporting burden
- Enables investors, lenders, and other financial statements users to compare financial performance among NPAEs
- Don't find anything particularly attractive

When IFRS-NPAEs is finalized, which best describes the direction of your company?



- Have no plans to adopt until full IFRS is mandated for U.S. public companies
- Will assess the costs/benefits of adoption
- Will consider adoption in the near-term
- Have no interest in adoption
- Don't know/not applicable

[5] Source: Private Company Dbriefs webcast, "IFRS: Why Private Companies Should Take Note," with over 1700 financial executives, held on January 28, 2009. Polling results represent the thoughts and opinions of webcast participants and are not necessarily representative of the total population of finance professionals.

Technical Corner: IAS 37

Accounting for Contingencies

The accounting for contingencies is an area of significant judgment. U.S. GAAP and IFRS both determine the required level of recognition and disclosure based upon the probability of an event occurring. However, there are differences between U.S. GAAP (SFAS 5, "Accounting for Contingencies") and IFRS (IAS 37, "Accounting for Contingencies) that could lead to different accounting treatments (i.e., recognition or disclosure) or recorded amounts.

- **Threshold** — Under IFRS, a provision is recorded when it is "more likely than not" that an outflow of resources will be required to settle an obligation. U.S. GAAP uses the higher threshold of "probable" when determining whether or not to record a liability.
- **Measurement of Provisions**
    - *Range of estimates* — IAS 37 requires obligations to be recorded at their best estimate, whereas SFAS 5 requires the most probable outcome be recorded. Moreover, if no one result is greater than another within a range, the mid-point and low-end of the range are recorded respectively for IFRS and U.S. GAAP.
    - *Discounting* — If the timing of related cash flows is fixed and determinable, then discounting is permitted under SFAS 5. Meanwhile, if discounting is considered material to the obligation then it is required under IAS 37.
- **Decommissioning Provisions**
    - *Initial measurement* — Under IFRS, asset retirement obligation (ARO) liabilities are measured as the best estimate of an expenditure to settle the obligation or transfer it to a third party at the end of a reporting period. Meanwhile an ARO liability under U.S. GAAP is measured at fair value in the period it is incurred.
    - *Discount rate* — IFRS utilizes the current risk-adjusted rate, as revised at each reporting date, to measure the provision. U.S. GAAP uses the credit adjusted risk-free rate to discount the liability, and it is not adjusted in future periods.
- **Restructuring Costs** — IFRS focuses on the exit plan as a whole and recognizes a liability if a detailed restructuring plan has been announced or has been started. In comparison, U.S. GAAP examines each type of exit cost individually and they are recorded when a transaction or event leaves an entity little or no discretion to avoid settling the liability.
- **Disclosures** — In extremely rare circumstances, the general details of a dispute may seriously prejudice the entity's position and therefore, under IFRS, the entity need not disclose them, but rather only the general nature of the dispute and reason that information is not disclosed. No such exemption exists with U.S. GAAP.

It is important for entities to ensure there is a strong understanding of the risks and uncertainties associated with each potential liability. Additionally, when considering an IFRS conversion, companies should be cognizant of the accounting differences and should thoroughly examine their accounting policies related to recognition and measurement of contingencies.

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