# Staff Observations in the Review of IFRS Financial Statements

### July 2, 2007

Filings made with the SEC are subject to staff review. In 2006, the staff reviewed the annual reports of more than 100 foreign private issuers containing financial statements prepared for the first time on the basis of International Financial Reporting Standards, commonly referred to as IFRS. Consistent with our normal practice, we asked some companies to provide us with additional information and we asked other companies to revise their financial statement presentation or enhance disclosure in future filings. In a limited number of comment letters, we asked companies to amend the reviewed filing. Our comment letters and company responses to those comment letters are available on the SEC website at www.sec.gov/divisions/corpfin/ifrs_reviews.

In this report, we discuss the principal areas of staff comment and note some general observations about the application of IFRS. We have not yet assessed application of any particular standard of IFRS, IFRS in its entirety, or the overall quality of disclosure in these reports. This summary does not include all areas in which we raised comments or asked questions nor does the order in which we present the topic areas signify their importance to an understanding of a company's financial condition or the frequency with which we raised comments. Finally, we have not yet reached any comprehensive conclusions about companies' overall compliance with, or consistency in application of, IFRS.

## Assertion of Compliance with IFRS

We found that the vast majority of companies asserted compliance with a jurisdictional version of IFRS and that most also asserted compliance with IFRS as published by the International Accounting Standards Board, commonly referred to as the IASB. In the vast majority of the companies we reviewed, the company's auditor opined on the company's compliance with the jurisdictional version of IFRS that the company used, but did not opine on the company's compliance with IFRS as published by the IASB.

We noted a number of variations in the language companies and their auditors used to describe IFRS as applied in the financial statements. We raised comments where this language appeared to be inconsistent with the explicit and unreserved statement of compliance with IFRS as called for by

IAS 1, Presentation of Financial Statements, and Instruction G to Form 20-F. We asked a number of companies to make the necessary assertion, or a clearer assertion, regarding compliance with IFRS as published by the IASB.

**Manner of Presentation**

We found that companies based in the same jurisdiction and companies in the same industries sometimes used different income statement formats. IAS 1 provides general guidance of minimum line items a company must include and requires a company to present other items, captions and subtotals "relevant to an understanding of the entity's financial performance." We asked a number of companies to:

- rename income statement subtotals so it was clear what each subtotal represented;
- explain the accounting policies they followed in determining what items to exclude from the income statement subtotals, including what elements constituted operating income; and
- disclose how they calculated additional voluntary per share measures and how they reconciled these measures to the income statement.

It is important to note that while we sought further explanation of the relevance of an item a company presented on the face of its income statement or in footnotes, we did not request any company to remove any measure that we would consider a non-GAAP measure under U.S. GAAP.

Regarding the presentation of statements of cash flows, we raised comments where a company used a starting point other than what IAS 7, Cash Flow Statements, permits, or where a company inappropriately characterized items as cash equivalents or classified expenses of an operating nature, such as research or exploration expenses, as investing rather than operating cash flows.

We found that there was a range of accounting treatments for common control mergers, recapitalizations, reorganizations, acquisitions of minority interests, and similar transactions. We asked a number of companies to provide us with information and enhance their disclosure about the manner in which they accounted for these transactions and the impact of the accounting treatment they selected.

We asked companies to support their conclusions and provide further clarification in the notes to their financial statements when it was unclear why a company did or did not consolidate a subsidiary or use the equity method of accounting.

When a standard or interpretation of IFRS does not address a matter, IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, requires companies to look to the most recent pronouncements of other standard-setting bodies. Where a company looked to other standard-setting bodies, we asked it to identify, in the accounting policy footnote to its financial statements, what standard-setting body pronouncements it relied upon. Consistent with IAS 8, we raised comments where a company indicated that it was relying on a standard-setting body pronouncement that appeared to be inconsistent with IFRS or the IASB *Framework*.

We noted substantial variation in accounting for insurance contracts and in the reporting of extractive industry exploration and evaluation activities in the absence of an extensive standard in IFRS for these activities, and raised comments as appropriate.

**Topical Areas**

We noted instances of a company scattering disclosure that IFRS requires on a topic among a number of locations in the filing, including locations outside the audited financial statements. In those instances where required topical disclosure was missing, unclear or generic, we raised comments.

We asked a number of companies to provide additional information or disclosure about:

- revenue recognition, especially where a company provided generic policy disclosure and did not provide disclosure specific to its circumstances. When a company did not address all material revenue-generating activities, we asked it to do so. In some instances, we asked questions about the scope and timing of revenue recognition;

- intangible assets and goodwill, including the factors that led a company to recognize them in a business combination;

- their policies for identifying and evaluating impairment, the circumstances resulting in recognized impairment, or the circumstances surrounding impairment reversals of long-lived assets including goodwill;

- leases, including their terms and the future minimum payments under operating and financial leases;

- contingent liabilities, including their nature and estimated financial effects; and

- the significant terms of financial instruments, including derivatives, their effect on future cash flow and the recognition and measurement criteria the company applied.

We questioned whether various banks complied with IAS 39, Financial Instruments: Recognition and Measurement, in determining loan impairment. Our discussions on this topic are ongoing.

*http://www.sec.gov/divisions/corpfin/ifrs_staffobservations.htm*

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