History and Background

The movement toward adoption of a single set of high-quality global accounting standards for use by organizations around the world continues to gather momentum in the U.S. and around the globe.

In the U.S., this movement began to take hold in 2002, when the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) issued the so-called Norwalk Agreement, in which they acknowledged their commitment to developing high-quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. The two bodies have been working together towards that end, in a process referred to as “convergence,” ever since.


In 2007, the U.S. Securities and Exchange Commission (SEC) adopted rules to accept from Foreign Private Issuers their financial statements prepared in accordance with IFRS as issued by the IASB without reconciliation to U.S. GAAP. Also, the SEC published a “Concept Release” to obtain information on allowing U.S. issuers to prepare financial statements in accordance with IFRS – which are not yet “converged” with U.S. GAAP – for purposes of complying with the rules and regulations of the SEC. Congress, which has the ultimate authority, is likely to become involved in the debate.

As of late 2007, nearly 100 countries require or allow the use of IFRS, and others are planning to do so in the near future. The SEC is exploring the use of IFRS for publicly traded U.S. companies.

Why Should Audit Committees Be Concerned Now?

While the SEC has not given U.S. companies a choice to file using IFRS, they are now exploring the use of IFRS for U.S. companies. And, given the SEC’s support for a single set of global accounting standards, it is reasonable to believe the SEC may require adoption of IFRS by U.S. registrants by a date certain in the not-too-distant future. Therefore, it is important that audit committees gain an understanding of IFRS – and also be prepared to ask their companies’ management a number of questions (see IFRS Considerations and Questions for Audit Committees tool, page 2) to determine their readiness, if given a choice for adoption of – or if they are required to adopt – IFRS.
Overview of IFRS First-time Adoption by a Company

- IFRS 1 provides detailed guidelines for first-time adoption of IFRS.
  - It requires an opening IFRS statement of financial position at the date of transition to IFRS.
  - There are 10 optional exemptions from retrospective application of particular accounting requirements and 4 mandatory exemptions prohibiting retrospective application.

- It requires an entity to comply with each IFRS effective at the end of its first IFRS reporting period.
- It requires disclosures that explain how the transition from U.S. GAAP to IFRS affected the entity’s reported financial position, financial performance and cash flows.

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS): CONSIDERATIONS AND QUESTIONS FOR AUDIT COMMITTEES

PURPOSE OF THIS TOOL: International Financial Reporting Standards (IFRS) are being used worldwide by nearly 100 countries that either require or allow its use for the preparation of financial statements for publicly held companies. Convergence of U.S. GAAP with IFRS is happening. In addition, there is a possibility that the SEC will give U.S. companies an option to follow IFRS rather than U.S. GAAP or require them to switch to IFRS, before convergence is achieved. Audit committees should anticipate this significant change and inquire of the CEO and CFO as to the readiness of the company, and their implementation plan for moving to IFRS if/when required.

Some considerations for filing of IFRS financial statements:
- Multinational companies may benefit from the use of common financial reporting systems that follow IFRS worldwide
- IFRS may ease financial statement comparability with other companies that use IFRS worldwide
- IFRS is intended to facilitate cross-border investments and access to global capital markets

Questions the audit committee should consider in its own deliberation include:
- Has the audit committee discussed the adoption of IFRS with the company?
- Does the audit committee feel that management understands how IFRS adoption will affect the company and its financial reporting process?
- Does the audit committee feel that management understands the full extent of the changes to the company and its financial reporting process?
- Does the audit committee have an oversight plan for IFRS adoption by the company for implementation and progress?
- What impact does IFRS adoption have on the ongoing responsibilities of the audit committee for internal control and financial statement disclosures?
- How will the audit committee members become financially literate on IFRS and learn the key differences between IFRS and U.S. GAAP?
• How will the audit committee understand and question the accounting policy choices made by management on the transition to IFRS? IFRS contains less detail than U.S. GAAP and their application may require more professional judgment. Therefore, it will take the company some time to evaluate its choices for accounting policies. Also, depending upon the accounting policy chosen, processes and/or systems (e.g., fixed assets, share-based systems, inventory, others) may be affected.

• How will the audit committee inform the board of directors and the compensation committee, etc., about the impacts of the company’s transition to IFRS?

• How will the audit committee know if management’s education goals for shareholders and analysts are being met?

**Questions the audit committee should review with management include:**

- Are any of the company’s foreign subsidiaries or joint ventures currently using IFRS?
- Has the company done a readiness assessment of IFRS adoption?
- What are the challenges, risks and cost/benefits of IFRS adoption?
- What is the level of knowledge of IFRS within the company?
- What type and level of education on IFRS will be needed by the company’s employees and other stakeholders?
- What steps should the company be taking to prepare for adoption of IFRS if an option is granted?
- Does the company have a transition plan (e.g., assessment, conversion, sustain) that includes key conversion activities (IFRS 1- First-time Adoption of IFRS, etc.), timetable and resources required, as well as project and change management?
- If IFRS is adopted, how will this affect the company’s way of doing business (e.g., changes to IT and other internal systems; risk monitoring and controls; relationships with external companies; contractual arrangements; outsourcing arrangements; inventory accounting; budgeting and forecasting; key performance indicators; compensation; joint ventures and alliances; subsidiaries; legal issues; etc.)?
- What are the changes to accounting policies and other policies? What is the potential financial impact of those changes? Is there an accounting impact on the defined pension plan? Are there any off-balance sheet items that would be brought on to the balance sheet or vice versa? What are the disclosure impacts?
- Are there any process or contract changes resulting from differences in hedge accounting guidelines?
- What are the tax impacts of IFRS adoption (e.g., pre-tax income; differences in tax accounting on a company’s effective tax rate; the company’s cash taxes in U.S. and foreign jurisdictions; tax-reporting processes; etc.)?
- What are the treasury (e.g., debt agreements and financial covenants, dividend policy, etc.) impacts of adoption to IFRS?
- How is management making system changes or implementing new systems today, in recognition of possible changes in the future?
- How is management implementing new accounting standards today, in recognition of possible changes in the future?
- Are there particular accounting issues under IFRS for the industry in which the company operates (e.g., insurance, oil and gas, etc.)?
Will external advisors be used to help with the transition to IFRS, and what are their qualifications and roles?

What is the company’s approach to identifying issues, resolving the issues and communicating this information to the audit committee?

What is the company’s plan on education of stakeholders (e.g., investors, analysts, lenders, creditors) so they understand the changes to the accounting policies and the financial statements? How will the company handle the restatement of comparative periods and its possible impact on investors?

What is the company’s plan for communicating to stakeholders regarding the transition to IFRS?

Has a formal risk assessment been documented with respect to IFRS? Has the IFRS risk assessment been integrated with existing risk assessment information?

RESOURCES
For additional information, visit these Web sites:

- **AICPA**
  - For the latest information on the status of IFRS and educational opportunities visit www.ifrs.com

- **IASB**
  - Memorandum of Understanding with the FASB:
    - http://www.iasb.org/CurrentProjects/Memorandum+of+Understanding+with+the+FASB.htm
  - IFRS summaries:

- **FASB**
  - Overview of International Activities: http://www.fasb.org/intl/

- **SEC**