IFRS vs. Convergence: Three Findings and Three Actions to Take Now

Arthur F. Rothberg, Managing Director, CFO Edge, LLC

With many significant FASB/IASB reporting convergence projects approaching completion by the targeted June 30 date, the stage is set for a likely Q3 or Q4 2011 statement by the Securities and Exchange Commission that will resolve whether U.S. public companies will be required to report under International Financial Reporting Standards (IFRS).

If the statement does not make IFRS reporting mandatory, it will provide needed clarity on how continued reporting under U.S. GAAP will be combined with convergence between FASB and IASB standards. In the meantime, there is certainty that U.S. companies be well-versed in IFRS given adoption by over 100 countries to date.

Until the ruling is issued, forward-thinking companies ponder the outcome and ask, what should we be doing now? This brief looks at three findings related to current perspectives on IFRS and suggests three actions companies can engage in to increase preparedness for the ruling later this year.

Findings
A review of recent developments and comments reveals varied IFRS perspectives from three groups of interested parties.

1. U.S. business executives' and professionals' perspectives
While most U.S. business executives and accounting professionals agree that GAAP and IFRS convergence is desirable, opinions on full-scale adoption of IFRS are more varied.

Favoring IFRS adoption
Those in favor see multiple benefits when everyone is speaking the same financial language. Advantages include the following:

Reduced costs – Current requirements to prepare multiple formats based on location sometimes require additional resources using disparate accounting systems at the local level. One standard would support consolidation of resources and systems to potentially reduce reporting and compliance costs.

Enhanced controls – One standard would support centralized reporting ownership and potentially result in improved global statement accuracy and quality.

Improved comparability of information – One standard would lead to greater transparency related to operational performance, valuations, and management accountability.

True "apples to apples" comparisons – One standard would provide investors with comparable data needed to make informed decisions, as well as promote efficiencies for companies seeking to raise capital in global markets.

Greater competitiveness – One standard has the potential to increase international competition and spur the global economy by making it less costly for U.S. companies to do business overseas and for foreign companies to compete in the U.S.

Reservations about IFRS adoption

While acknowledging benefits from progressive convergence at a measured pace, many executives and professionals are reluctant to support full-scale IFRS adoption based on the following:

Importance of a rules-based approach – Citing past experiences with Enron and WorldCom when companies were allowed to report based on interpretations, many have expressed preference for the U.S. GAAP rules-based approach over the IFRS principles-based approach. Concern is voiced that a move to an IFRS standard will lose the surety that currently accompanies compliance with the U.S. GAAP standard.

IFRS countries are adopting exceptions – Some observe that a number of the over 100 countries that have adopted IFRS are applying local exceptions and that this move will prevent global adoption

Burden for privately-held and small companies – Concern has been expressed that IFRS adoption is costly and unnecessary for smaller and closely-held companies that don't do business abroad.

Move to IFRS is too fast – Encouraging a more deliberate pace in assessing impact and applying IFRS, some say that the move to implement is happening too quickly.

Asked in a February Q&A if the SEC will continue to move toward adopting IFRS, AICPA President and CEO Barry Melancon replied with the following comments:

"Yes, I believe it will. The current IFRS Work Plan is aimed at making a decision this year about setting a date certain for IFRS adoption, which would not take place before 2015.

"This is an emotional issue for the United States. Given the weak economy, coupled with the high cost of converting to IFRS, adoption might slip beyond the 2015 tentative date in the SEC's work plan. Still, the SEC has said it remains committed to a decision sometime in 2011.

"The vast majority of countries around the world are adopting IFRS, but they also have reserved the right to make modifications to take into account factors unique to their country. Most countries, while they have reserved the right to make changes, have not in fact made them.

"I think what the U.S. does will go a long way toward deciding which way this goes." [1]

The AICPA's IFRS Readiness Survey (October 2010)[2] asked member CPAs if they believed ultimately the SEC should require adoption of IFRS for U.S. public companies, and results* follow:

15%:	Yes
40%:	Yes, but only after more convergence
21%:	No, but IFRS should be an option
8%:	No, IFRS should not be mandated or allowed
17%:	Unsure

** Percentages may not sum to 100 due to rounding error.*

Of all survey participants that responded, 39% said they are delaying IFRS preparations pending the SEC decision.

2. SEC perspective

The Securities and Exchange Commission is committed to a 2011 decision as to whether it will require IFRS implementation, although Mary Schapiro, SEC Chairman, noted in a December 2010 talk at the AICPA National Conference that it is not committed to a decision by June 2011. If the SEC does require IFRS adoption, it is positioning 2015 or 2016 as the timeframe for implementation.

Also at the AICPA National Conference, Paul Beswick, SEC Deputy Chief Accountant, responded to a question about what the model would look like if the SEC incorporates IFRS into U.S. requirements with the following comments:

> *"In our October update we highlighted that the majority of jurisdictions are following either a convergence or an endorsement approach. In my opinion, if the U.S. were to move to IFRS, somewhere in between could be the right approach. I will call it a 'condorsement' approach.*
>
> *"U.S. GAAP would continue to exist. The IASB and the FASB would finish the major projects. The FASB would not begin work on any major new projects in the normal course. Rather, a new set of priorities would be established where the FASB would work to converge existing U.S. GAAP to IFRS over a period of time for standards that are not on the IASB's agenda."* [3]

He noted this combined and deliberate approach…

- Upholds the quality of existing U.S. standards
- Assures IFRS standards are suitable for U.S. markets on a standard-by-standard basis
- Minimizes the cost to U.S. companies and investors
- Provides time to understand complex facts and circumstances
- Supports review of potential impact on laws, reporting, and corporate governance

3. IASB & European Commission perspectives

March 2011 statements from IASB and the European Commission expressed concern about delays in U.S. IFRS adoption.

A recent CFO.com article quoted IASB chairman David Tweedie as saying that a U.S. delay in committing to IFRS beyond 2011 would cause companies here to incur unnecessary costs and also risk divergence in standards:

> *"The window of opportunity will close if a decision is delayed. At the same time, a decision this year will provide U.S. companies, auditors, and educators with the necessary certainty and time they require to prepare."* [4]

And a recent Financial Times article referenced this European Commission's statement on the pace of U.S. ratification:

> *"Convergence between IFRS and US accounting standards imposes costs on EU companies that are increasingly difficult to justify without a firm commitment by the US to IFRS."* [5]

The article also noted European comments that not committing to IFRS could both put U.S. IASB participation at risk and cause the U.S. to lose international influence.

Actions to take now

With U.S. opinions split on the value of IFRS adoption and many delaying action until the SEC decision is announced, what should a forward-thinking company do now?

1. Assess IFRS impact, set objectives, and prepare for transition

Known are that an SEC decision is likely in Q3 or Q4 2011 and that changes in reporting requirements will occur as a result.

Unknown are what changes will be mandated and precisely when, although the SEC is looking at 2015 as a potential implementation timeframe. Until this information becomes available, companies should be engaged in assessment, readiness planning, and preparation.

The significant complexities, challenges, and costs associated with conversion warrant creation of an IFRS project team comprised of representatives from key stakeholder groups. The team should determine what impact potential conversion will have on the following areas: personnel; global customers and suppliers; applications and systems; controls; processes and procedures; reporting content and format requirements; exposure factors; tax liabilities; and contracts.

Efforts should also be directed at identifying critical success factors, critical risk factors, objectives, strategies, and actions that will support a transition to new reporting requirements.

By taking a proactive approach to thoroughly understand the pervasive requirements and effects of an IFRS transition, companies will be better prepared to implement changes when the direction and timing become clear.

2. Identify "what if" scenarios and stay informed

Based on IFRS project team findings, companies should create "what if" scenarios that address potential IFRS/convergence outcomes. These scenarios can even be weighted by probability of occurrence based on the project team's due diligence.

For example, a project team may determine the following are three likely outcomes, each with an equal probability of occurring:

1. The SEC will affirm the primacy of U.S. GAAP and support continuing convergence.
2. The SEC will mandate adoption of IFRS for U.S. public companies.
3. Countries in which companies have subsidiaries will soon adopt IFRS.

In this example, the project team will essentially develop three game plans that set forth requirements, strategies, and action items unique to each. As 2011 progresses, new information will elevate probable occurrence for some options and eventually clarify direction based on the SEC decision.

Up-to-date sources for IFRS and convergence developments include the following:

SEC.gov: Spotlight on Work Plan for Global Accounting Standards
www.sec.gov/spotlight/globalaccountingstandards.shtml

AICPA.org: IFRS Articles, Newsletters, and Publications
http://www.aicpa.org/_catalogs/masterpage/Search.aspx?S=ifrs

IFRS.com: AICPA IFRS Resources
http://www.ifrs.com/

IFRS.org: IFRS Foundation and IASB
http://www.ifrs.org/Home.htm

FASB.org: Financial Accounting Standards Board
http://www.fasb.org/

Some offer subscriptions to email newsletters with content focused on IFRS news, and some provide Twitter updates.

3. Gap analysis: available vs. needed resources and systems
The IFRS project team's work should also include a gap analysis to determine the extent to which current resources and systems will need to be augmented to address the IFRS "what if" scenarios identified in the previous section.

Determinations should be made regarding whether current personnel have sufficient skill sets and bandwidth to implement and support new reporting requirements. Where there is a gap, planning should address the addition of FTEs, IFRS-specific training, and consultants or other outside resources with needed expertise.

IFRS reporting will also generate challenges around financial reporting applications and systems. Reporting areas to be addressed include the types of information needed, volume, frequency, input sources, output formats, and resource responsibility and accountability. Of particular importance is the extent to which business users can exercise control over needed changes vs. business users needing to contact IT to request modifications.

An IFRS/convergence holy grail reporting system would be a current system capable of both satisfying existing reporting requirements and meeting changes mandated by new requirements, whatever they may be. In the absence of this ideal solution, the project team will also need to examine the cost/benefit ratio of modifying current systems or adding new ones.

Planning should also address how changes impact resource and system requirements when the company has operations, customers, or suppliers in countries that either have already adopted IFRS or will do so in the near future.

A transition to IFRS presents a large number and wide variety of complexities, challenges, and costs. Conversions on this scale cannot be accomplished in short timeframes that are deadline driven, and doing so only serves to increase costs and exposure risks. Forward-thinking companies will create a dedicated project team that will engage in a process of assessing requirements and developing strategies to successfully address the approaching mandate, regardless of whether that is IFRS- or convergence-based. This proactive, front-loaded approach is essential to controlling costs, as well as growing profitability and shareholder value.

1. A Q&A with AICPA President & CEO Barry Melancon, CPA; AICPA.org; February 23, 2011; www.aicpa.org/News/FeaturedNews/Pages/AQAwithBarryMelancon.aspx
2. IFRS Readiness Tracking Survey | October 2010; AICPA.org; www.aicpa.org/Research/StudiesandPapers/DownloadableDocuments/IFRS%20Readiness%20Survey%20--Fall%202010%20--%20Public%201013.pdf
3. Speech by SEC Staff: Remarks before the 2010 AICPA National Conference on Current SEC and PCAOB Developments; Paul A. Beswick, Deputy Chief Accountant, U.S. Securities and Exchange Commission; Washington, D.C.; December 6, 2010; www.sec.gov/news/speech/2010/spch120610pab.htm
4. Tweedie Pushes for IFRS Decision This Year; David M. Katz, CFO.com; March 11, 2011; www.cfo.com/article.cfm/14562111/c_14562328
5. Brussels pushes US on accounting; Adam Jones; Financial Times; March 6, 2011; www.ft.com/cms/s/0/0c9f7c38-4834-11e0-b323-00144feab49a.html#axzz1HYmyIZeD (registration required)

About CFO Edge

CFO Edge is a leading Southern California provider of interim CFO services. We are a group of experienced chief financial officers who engage with CEOs and CFOs on demand to address strategic planning, business management, and day-to-day financial operations challenges. Our seasoned professionals deliver services as interim CFOs, part-time CFOs, project-based CFOs, recruitment-to-permanent CFOs and interim-to-permanent CFOs. At CFO Edge, we're passionate about helping our clients create, grow and sustain value. For more information, please send an inquiry via our Contact page at www.cfoedge.com or call 626.683.8840.

