

International Financial Reporting Standards (IFRS)

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Are you ready for IFRS?

The acceptance of International Financial Reporting Standards (IFRS) as the preferred method of financial reporting on a global level leaves U.S. companies and accounting firms with many fundamental changes that will transform their traditional accounting models. Approximately 113 countries permit or require the use of IFRS for the preparation of financial statements for publicly held companies with several others planning convergence in the next several years.

Why or why not converge to IFRS?

The globalization of business and finance has led to a growing interest in a single set of international accounting standards. Using IFRS, companies and regulators feel that they will now have the ability to compare financial results across multiple country jurisdictions since they will all be using the same accounting standards. This will allow investors to understand and explore additional international opportunities. A 2007 survey conducted by the International Federation of Accountants, which included 143 leaders from 91 countries, found that more than 90% of the respondents agreed that a single set of international financial reporting standards was important for economic growth for their country.

Opponents of the convergence project express concerns that important financial information will be lost with implementation of IFRS. Many believe that U.S. Generally Accepted Accounting Principles (GAAP) is the “gold standard” of reporting. IFRS does not require near the level of detail for financial reporting as does U.S. GAAP. For example, IFRS fits into one book about two inches thick while the Financial Accounting Standards Board (FASB) pronouncements and Emerging Issues Task Force consensus measures about nine inches thick and that does not even include authoritative literature. Worldwide, many countries that have converged to IFRS still have reserved the right to modify standards that they do not consider in their national interest. This could lead to incomparable financial statements, which is counter-productive toward the global adoption of IFRS.

What is happening in the U.S.?

In order to stay competitive in a global market, U.S. accounting regulators are taking action. On November 14, 2008, the Securities and Exchange Commission (SEC) released for public comment a proposed roadmap that provides a timeline and key milestones for adopting IFRS beginning in 2014 for public companies. As part of this project, regulators from the FASB and IASB are meeting to converge the content of U.S. GAAP and IFRS, as there are currently many differences in accounting treatment between the two standards. The goal of this project is to have most or all of the key differences resolved by the time the U.S. adopts IFRS.

Who will be impacted?

Although it is widely viewed that implementation of IFRS will only impact the accounting department of companies, the effect is far reaching. Implementation of IFRS will encompass a company's entire operations including auditing and oversight, cash management, corporate taxes, technology and software.

The impact of implementing IFRS is likely to surpass that of the Sarbanes-Oxley Act of 2002. Due to the expected implementation time, companies are suggested to begin preparing up to three years in advance. It is anticipated to take two to three years for companies to upgrade communications and software systems as well as train financial professionals.

Impact on financial reporting

In order to implement IFRS, accounting systems will have to be updated to handle increased disclosure and dual-reporting requirements. The first year of financial reporting under IFRS will require three years of audited financial statements. Therefore, companies will have to report the current year and two prior years under both GAAP and IFRS to comply with the new standards. Currently, many countries that have already implemented IFRS require a reconciliation of IFRS with the local country method of accounting for tax reporting.

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Impact on tax preparation

Implementation of IFRS will have a large impact not only on company financial statements, but also on tax reporting. For instance, differences between IFRS and GAAP will be new tax adjustments in the year of change. There are also numerous differences between IFRS and GAAP that will impact tax reporting including depreciable assets and inventory valuation.

IFRS prohibits the use of Last In First Out (LIFO) costing method to account for inventory. The adoption of IFRS for financial reporting could result in significant tax consequences. The stated preclusion of LIFO for financial reporting would violate current Internal Revenue Service (IRS) conformity requirements for those using LIFO for tax purposes.

The impacts of adopting IFRS will affect not only federal tax reporting but state tax filings as well. The differences in depreciable assets and inventory valuation will affect state apportionment calculations and other indirect or state franchise taxes.

What should companies do now?

Although it may be several years before the U.S. fully adopts IFRS, the standards are already having a significant impact on U.S. businesses. More and more U.S. companies transact business with a global customer or supplier base, many of which are located in a country that has already adopted IFRS. U.S. companies with a solid understanding of IFRS will be in a better position for business negotiations ranging from sales and purchases to mergers and acquisitions.

In the short-term, companies should focus on continued understanding of the differences between IFRS and GAAP, monitoring adoption of IFRS by other countries for future business dealings, and understanding the ways in which the structure of transactions with non-U.S. counterparties may be influenced by increased interest in IFRS.



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