Trends

What Do You Need To Know About IFRS?

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International financial reporting standards (IFRS) are here:[1] The SEC now accepts IFRS as issued by International Accounting Standards Board (IASB) from foreign company registrants. Further, the AICPA says that IFRS are high quality accounting standards under the ethics code and may be used currently by non-registered private companies in lieu of U.S. GAAP. Also, the SEC has announced a roadmap to decide in 2011 whether registered public companies are permitted or will be required to use IFRS as a substitute for U.S. GAAP as early as 2014.[2] One clear conclusion from these developments is that, for at least a period of time, knowledge of both U.S. GAAP and IFRS will be required. Since most business students take only beginning accounting, IFRS is not a subject that can be reserved for upper level courses. IFRS must be integrated into the curriculum starting with the first accounting course. What do you as an accounting instructor need to know about IFRS? And what should you tell your students?

Here are some basics about IFRS: International financial reporting standards (IFRS) are accounting standards issued by the IASB based in London. The IASB consists of fourteen standard setters who have technical expertise. The IASB meets one week per month. Versions of IFRS are used in more than 100 countries including all European Union countries, Australia, Argentina, and Brazil. By 2011, it is expected that all major countries, including China, India, Japan, Canada and the U.S., will have adopted or converged to IFRS.

The perceived benefits of IFRS are:

- Enhanced comparability of financial statements
- Improved corporate transparency
- Increased quality of standards
- Potentially lower cost of capital
- Reduced costs of preparing statement on multiple standards
- More discretion to convey superior information

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[1] Securities and Exchange Commission, "Rules and Regulations," *Federal Register*, Vol. 73, No. 3, January 4, 2008
[2] "SEC Unanimously Approves Exposing Proposed IFRS Roadmap for Public Companies, www.AICPA.org, August 27, 2008.

The SEC believes the ideal outcome is the worldwide use of a 'single' set of high quality accounting standards for both domestic and cross-border financial reporting. In reality, consistency does not now exist. Therefore, for a period of time, users of financial statements will have difficulty comparing companies' performance. When foreign firms filing in the U.S. use IFRS, profitability measures will not be comparable to companies using U.S. GAAP. For instance, the reporting earnings of these European companies under both standards in a recent year illustrate that reported earnings will vary.

	IFRS Earnings	**GAAP Earnings**	**% Difference**
Bayer AG	1,695	269	530.1%
Reed Elsevier	625	399	56.6
Benetton Group	125	100	25.0

Earnings in millions of Euros

Also, differences in the uses of fair value in valuing assets and liabilities will alter assets and equity and resulting profitability ratios—profit margin, asset turnover, return of assets, and return on equity. Further, IFRS differs from U.S. GAAP in debt versus equity classification on the balance sheet and income statement format and classification. In addition, numerous differences in individual areas cause these performance measures to lack comparability. A few of them are the following:

- Revenue recognition
- Intangible assets
- Impairment
- Reevaluation
- Share-based payments

Other concerns about mandating IFRS also exist: 1) transition to IFRS may be costly; 2) cultural differences may result in different applications of the standards; 3) significant changes are needed in the curriculum and the CPA examination. IFRS are designed to be "principles-based" without the detailed rules that accompany U.S. GAAP. The result will likely mean more judgment in application of IFRS and increase litigation in U.S.

In summary, there are a wide variety of differences including the following:

- Concepts (no matching principle or conservatism under IFRS)
- Level of detail (revenue recognition)
- Approach to industry specific guidance (entities versus activities)
- Scope (employee share compensation versus all-share-based payments)

In conclusion, the move to IFRS has not altered plans of the IASB and FASB to work toward convergence of standards. By 2011, fewer differences in U.S. GAAP and IFRS are likely but some areas will be difficult to reconcile. One example, IFRS do not allow for LIFO accounting for inventories, which is the most popular method used in the U.S. Your students in the first course must be aware of IFRS, but IFRS should not displace traditional GAAP at this time. The basics of IFRS should be integrated at appropriate points in the course and not relegated to a separate chapter. For example, in covering chapter 1, students should be informed that there are now two accepted standard-setting bodies, the FASB and the IASB. Further, students should know they will encounter IFRS in the future. Knowledge of the history, status, benefits, and disadvantages of IFRS is important. At appropriate points in the course, plan to mention the major areas where IFRS differs from GAAP.