

PKF PERSPECTIVES

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Most likely, you have heard the term “IFRS” (commonly pronounced “Eye-Fers”) which is the acronym for International Financial Reporting Standards. They are a set of accounting standards issued by the International Accounting Standards Board (IASB) which have been adopted by some 100 countries as the basis of their national accounting standards. The United States is one exception and has not adopted them.

In a “nutshell,” IFRS are “principles-based,” whereas Generally Accepted Accounting Principles in the United States (U.S. GAAP) are “rules-based”.

From an historical perspective, IFRS had been called International Accounting Standards (IAS) and were issued between 1973 and 2001 by the International Accounting Standards Committee (IASC). In April 2001, the IASB, which replaced the IASC, adopted all the IAS (those issued before 2001) and called the new standards (those issued after 2001) IFRS. Although IAS are no longer written, they are still in effect either partially or in their respective individual entirety, unless replaced by a new IFRS.

IFRS have been endorsed by the International Organization of Securities Commissions (IOSCO) and mandated for consolidated financial reporting in the European Union (EU).

Steady Progress on Convergence

At a 2002 meeting of the IASB and the U.S. Financial Accounting Standards Board (FASB), it was agreed that each would work toward reducing the differences between IFRS and U.S. GAAP. At their meetings in April and October 2005, the IASB and the FASB re-affirmed their commitment to convergence.

One underlying difference between the two standards is that U.S. GAAP has highly specific rules, while IFRS relies more on judgment, which may lead to differing conclusions. Because U.S. GAAP has been in existence much longer than IFRS, the body of interpretive literature related to U.S. GAAP by standard-setters and industry groups prescribes specific requirements for certain transactions, whereas IFRS may require more analysis of guidance and general principles that are presently available.

To provide a sense of some of the matters that require attention by the IASB and the FASB in their quest for convergence, the following are just a few:

- Revenue recognition
- Leases
- Business combinations
- Financial instruments
- Impairment
- Consolidation
- Segment reporting

Securities and Exchange Commission (SEC)

Under current SEC rules, foreign private issuers may file their financial statements in the United States using IFRS, their national GAAP or U.S. GAAP. However, if the foreign registrant reports in other than U.S. GAAP, it must provide a reconciliation of those financial statements in U.S. GAAP. Six months after its year-end, a foreign issuer must file its annual report, including financial statements, reconciled as appropriate to U.S. GAAP.

In April of 2005, Don Nicolaisen, then the Chief Accountant of the SEC, set forth a "roadmap" to a time anticipated to be 2009 when issuers that file their financial statements with the SEC may no longer be subject to reconciling their financial statements from IFRS to U.S. GAAP. Requisite benchmarks to such a time would include: (1) the convergence process between IFRS and U.S. GAAP; (2) faithful and consistent application of IFRS across borders; (3) comparability among and across users; and (4) appropriate, high quality auditing standards.

Heretofore, the SEC was a staunch proponent of the use of U.S. GAAP. Only recently has the SEC voiced its support of global accounting standards, probably in response to market forces and under the conditions enumerated above. Reconciliation of IFRS to U.S. GAAP is costly and ending it may produce benefits for investors, for issuers and for raising capital.

In a press release issued on April 24, 2007, the SEC announced a series of actions it intends to take this summer relating to the acceptance of financial reporting in IFRS, including a request for comments on proposed changes. SEC Chairman Christopher Cox stated that: "we remain on track to eliminate reconciliation [i.e., converting IFRS to U.S. GAAP when foreign registrants file their financial statements with the SEC] by 2009."

Conrad Hewitt, the SEC's Chief Accountant, added: "Whether foreign private issuers, and ultimately U.S. companies, should be permitted to use financial statements prepared using IFRS without the current reconciliation to U.S. GAAP are

important policy questions for the Commission and U.S. investors."

The White House Weighs In

President Bush, German Chancellor/European Union President Angela Merkel and European Commission President Joseph Manuel Barroso established the Transatlantic Economic Council (TEC). In a recent White House press release, it was stated that one of the TEC's goals is to "Promote conditions for the U.S. Generally Accepted Accounting Principles and International Financial Reporting Standards to be recognized in both jurisdictions [the U.S. and the EU] without the need for reconciliation by 2009 or possibly sooner."

The Case for U.S. GAAP

U.S. accounting standards are considered to be the most stringent, detailed and consistent in application. They have served as a model for international and national standards and have withstood the test of time, including accounting scandals. In addition, many foreign users of financial statements are familiar with U.S. GAAP.

It is the belief of many experts that IFRS should not necessarily replace U.S. GAAP, but be used in conjunction with it.

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June 2007