

IFRS...Are You Ready?

What to Think About and Take Action On Now

White Paper

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On Aug. 27, 2008, the U.S. Securities and Exchange Commission (SEC) voted to release the widely anticipated proposed roadmap to make International Financial Reporting Standards (IFRS) the generally accepted accounting standard in the United States. The proposed plan could require the largest U.S. public companies to begin reporting under IFRS as soon as 2014.

The plan to replace Generally Accepted Accounting Principles in the United States (U.S. GAAP) with IFRS is a fairly new and controversial one. The first serious proposal made publicly to move away from ongoing IFRS and U.S. GAAP convergence efforts and toward IFRS adoption was made in August 2007. The SEC solicited and received favorable feedback on possibly offering U.S. issuers a choice of preparing financial statements under U.S. GAAP or IFRS. In November 2007, the SEC permitted foreign private issuers who report under IFRS [as published by the International Accounting Standards Board (IASB)] to omit the reconciliation to U.S. GAAP.

The SEC's recent moves toward IFRS reflect a number of significant developments around the world in the last five years. These include significant growth of emerging economies and capital markets outside the U.S.; wide acceptance of IFRS (and forms of IFRS) around the globe (more than 100 countries have adopted IFRS); the growing complexity of accounting, reporting, and regulation of U.S. public companies; and other U.S. global economic and political factors.

With the recent developments, how are U.S. companies getting ready for this highly probable, ground-breaking change? Following are answers to important questions about the latest developments and the planned change to IFRS, as well as recommendations from SolomonEdwardsGroup's National SEC Advisory Practice on ways to prepare and take action now.

What did the SEC outline in its most recent proposed roadmap to IFRS and when is IFRS reporting expected to be mandated for U.S. public companies?

The SEC's proposal is expected to outline four milestones it will actively work toward and evaluate, with the expectation that these are substantially met before an IFRS mandate in the U.S. would occur. The anticipated milestones are:

1. Continued development of IFRS and ongoing progress on the convergence of IFRS and U.S. GAAP.
2. Improved accountability and agreement on the ongoing funding structure of the IASB.

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3. Development of an IFRS XBRL taxonomy. XBRL, an eXtensible Business Reporting Language approved in the U.S., is used to electronically tag financial information so as to simplify the retrieval, use, and comparability of accounting information. In May 2008, the SEC proposed that XBRL be required late this year for domestic and foreign large accelerated filers with a market capitalization in excess of \$5 billion. Under the current proposal, remaining U.S. GAAP reporting companies would be required to use XBRL over the next two years.
4. Continued training and education of investors, auditors, and preparers on IFRS.

Progress against the milestones will be reviewed in 2011, at which time, the decision to proceed with the IFRS mandate will be made. If the mandate is issued in 2011, it is expected that 2014 will be the first year large accelerated filers would be required to report under IFRS, 2015 for accelerated filers, and 2016 for all other filers.

The recent proposal also provides an opportunity for a limited number of companies to voluntarily adopt IFRS for years ending on or after Dec. 15, 2009. Early adoption must first be approved by the SEC by requesting a "no-objection" letter. Companies that are one of the 20 largest companies within an industry group which predominantly reports in IFRS will generally be permitted to adopt early.

The SEC's proposal has a 60-day comment period. Final rules are expected by year-end, depending on the volume and nature of the comments received.

What should I do to prepare for a likely move to IFRS? What actions should I take now and over the next few years?

At this time, monitoring current SEC developments related to IFRS is a good way to start preparing for the move. Increase your awareness and build on your familiarity with IFRS. Initiate planning and consider exploratory IFRS transition discussions with senior leaders within your organization.

Inform the leadership of your company, including the audit committee and board, about the recent developments on IFRS, including the anticipated timing of the IFRS transition for your company. Senior leadership will need to understand the depth and comprehensive nature of adopting IFRS to ensure a smooth and successful transition.

Plan to give the company and yourself sufficient time to implement. Implementing comprehensive, often complex, new accounting principles requires significant time and resources. Consider all key accounting and business processes, not just where U.S. GAAP and IFRS differences are expected. It may be prudent to apply IFRS to all accounting and business areas instead of working to minimize differences with U.S. GAAP. Also, while

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IFRS is more principle-based than U.S. GAAP, the requirements of Sarbanes-Oxley (SOX) remain relevant. Companies will need to prepare adequate documentation and perform adequate control testing under the new policies and methods in order to meet their SOX 404 and related requirements.

As the IFRS mandate and timing becomes more certain, begin more detailed planning with cross-functional leadership at your company. Develop a timeline of the planned transition to IFRS and when key actions will be taken. Secure board approval of the plan and the commitments made by leadership across the organization.

Discuss anticipated issues with the leaders of general counsel, tax, human resources, and information technology. All or most agreements currently in force at the company will need to be reviewed. As a first step, references to "U.S. GAAP" will need to be revised to specifically refer to "IFRS" or to a "generally accepted accounting standard" to provide added flexibility. Most contract provisions will need to be further examined to determine whether any economic terms or covenants are also impacted by the change to IFRS.

Contract provisions and measurements (such as key performance indicators, earnings measurements, asset valuations, and employee and executive compensation plans) measured using U.S. GAAP or tied directly or indirectly to U.S. GAAP may need to be amended or potentially renegotiated to safeguard the intended objectives. Additional provisions may be needed to achieve objectives previously addressed through the application of U.S. GAAP. Tax reporting requirements in various local jurisdictions may need to be closely reviewed to ensure ongoing compliance with the laws during the company's transition to IFRS. Accounting, HR and other information systems will need to be reviewed and modified to capture new IFRS accounting principles and methods as well as new information and disclosure requirements.

Inform your accounting team of the significant developments as well as the opportunities to learn more about IFRS and how they will be a part of the important change at the company. Look for IFRS training that provides an overview along with sufficient detail on specific accounting matters most relevant to your company.

Empower your accounting leaders to develop IFRS transition plans for the accounting areas they manage. Develop a process to review and approve the plans and to monitor implementation. Accounting professionals having familiarity with both IFRS and U.S. GAAP will become particularly valuable to your company.

Begin a two-way dialogue with your independent auditors. Provide the auditors with your plans for making the transition over the next several years and obtain their feedback and recommendations.

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Start to document the expected changes in accounting and non-accounting areas at your company. Begin to research known differences between IFRS and U.S. GAAP. While certain accounting principles may seem very similar, underlying measurements, calculations or other aspects of applying the principles may differ (impairment testing for long-lived assets, for example). Complete an IFRS accounting checklist to help perform and document the company's detailed review and comparison between U.S. GAAP and IFRS.

Initiate discussions with professional service providers, such as actuaries, tax professionals, and valuation advisors, who will need to make changes when providing information previously required in accordance with U.S. GAAP (e.g. pension accounting and related disclosures, SFAS 109 income tax accounting and reporting requirements, and tangible and intangible asset fair valuations).

Secure and build IFRS technical accounting and reporting expertise early. Technical resources will be in high demand in coming years; however, much of the upfront research and planning can be started early. Plan to support and retain valuable employees at your company during this new and significant transition. Provide additional support for your employees as they begin to take on new responsibilities related to IFRS deliverables in addition to existing duties. Let your employees know of the investments you are making in their future and the company's future and the new opportunities you are making available.

What changes are expected in the public filings for the transition from U.S. GAAP to IFRS? Will I need to provide a reconciliation or report several years under both IFRS and U.S. GAAP?

Additional guidance is expected in the final published rules. However, the SEC currently requires three years of income statements and two years of balance sheets to be included in annual SEC filings. As such, for companies beginning to report under IFRS in 2014, statements of operations, cash flows, and changes in equity for the years 2012-2014 are expected to be required. In addition, an IFRS opening balance sheet as of the beginning of 2012 (or Dec. 31, 2011 for calendar fiscal year reporting companies) would be required. Given the amount of research, planning, and education required, as well as the need for three years of IFRS results and reporting history, it is advisable to begin the planning process for conversion in the next one to two years and to keep in step with emerging IFRS-related SEC developments.

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What will the next few years under IFRS look like? Won't IFRS evolve back to a form of U.S. GAAP due to the growing complexity of the business world?

The drivers that lead to U.S. GAAP becoming a more complex set of accounting principles won't go away with the transition to IFRS. IFRS is expected to change significantly in coming years, but not necessarily in the direction of U.S. GAAP.

With one, truly global standard, countries around the world will be able to focus their efforts and resources to timely address the most pressing issues facing the global business and economic community. IFRS standards will be written to address wider sets of circumstances and are expected to continue to be more principles-based than U.S. GAAP (U.S. GAAP has been more rules-based and industry-specific). Accepted practices will continue to evolve over time, but generally, they may evolve in many new directions based on the evolving business issues and needs of the global economic community.

A Call to Action

IFRS is coming. Many parties working closely with the SEC anticipate the change will come quickly—in the next four to eight years. The more you do to prepare for this coming change will only help ensure a smooth and successful transition for you and your company in the years to come.

For more information about IFRS and obtaining assistance with the transition to IFRS, contact Brian Markley, managing director and SEC national practice leader for SolomonEdwardsGroup, at 312-466-0101 or bmarkley@solomonedwards.com.

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About SolomonEdwardsGroup

SolomonEdwardsGroup, LLC (SEG) is a national CFO services firm solving the shifting needs of CFO organizations and its professionals. It is recognized for delivering talent, perspective, and action in the critical areas of risk and regulations, resource management, accounting operations, and business performance.

Headquartered in Philadelphia, the firm operates offices in Atlanta, Chicago, Dallas/Fort Worth, Houston, Kansas City Metro, New York Metro, Philadelphia and Washington, D.C. Metro. Additionally, it maintains a global network of partners to serve multinational clients.

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