From *The Investment Professional,* Vol. 2, No. 1
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The Hard Sell

SEC IN A QUANDARY OVER ITS PUSH FOR IFRS

BY AMY E. BUTTELL

The seemingly unstoppable juggernaut of US IFRS (International Financial Reporting Standards) adoption has collided with the global financial crisis, one of the few barriers that may be capable of derailing the rush to a single international accounting standard. Adoption of IFRS in the US is now far from a given, and even the roadmap published by the US SEC (Securities and Exchange Commission) in November 2008 has the potential to be sidetracked or possibly abandoned now that President Obama's administration has taken office.

ILLUSTRATIONS BY MARK ANDRESEN

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Peter Bible, CPA, partner in charge at the public companies group of Amper, Politziner & Mattia

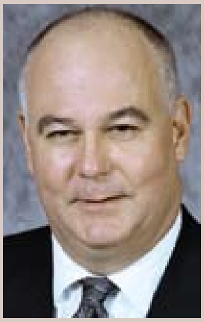
- Former chief accounting officer at General Motors
- Inaugural recipient of the Andrew Braden Award from Case Western University's Weatherhead School of Management
- Served as chairman of the Financial Executives International's Committee on Corporate Reporting

"I think users of financial information like to avoid excessive diversity in order to facilitate their job of making comparisons. When you have a set of standards that—I don't want to say 'encourages'—that allows for that diversification, I think it makes the job that much more difficult. It puts the onus back on the user to try to figure it out."

Jack Ciesielski, CFA, CPA, publisher of the Analyst's Accounting Observer

- Served on the Financial Accounting Standards Board's Emerging Issues Task Force, the Financial Accounting Standards Advisory Council, and the American Institute of Certified Public Accountants Accounting Standards Executive Committee
- Securities analyst, Legg Mason Value Trust, 1985–1992

"I think the question that has to be asked is, 'What is the downside if we don't move to IFRS now?' All the naysayers who say that failing to migrate will be the end of US markets—are they really right or are we doing something because we are afraid? Frankly, I think it would be good to have competition for a while. In the end, convergence is good, but let's stay on the path that we've been on, the evolution, where the FASB and IASB are working together and moving toward joint standards."



Patrick Daugherty, JD, chief strategy partner in the business law department of Foley & Lardner

- Served as counsel to SEC commissioner Edward Fleischman during the Reagan administration
- Tendered and qualified as an expert in securities law in criminal fraud proceedings brought by the US Department of Justice
- Led the team of attorneys that invented the Euro Currency Trust, the first currency-based exchange-traded fund

"I doubt that IFRS will be as high a priority as reform of the financial market regulatory structure in the US. That will be such an all-consuming task that IFRS will be subordinated. Regulation of accounting will take a back seat to the regulation of finance. So that will slow the potential adoption down."

In particular, the appointment of Mary Schapiro as chair of the SEC (a probable development when the *Investment Professional* went to press) bodes ill for supporters of a rapid adoption of IFRS, as Schapiro has expressed reservations about the timeline for IFRS adoption approved by the SEC under her predecessor, Christopher Cox. Still, there is substantial momentum on the side of IFRS. Paul Volcker, chairman of Obama's Economic Recovery Advisory Board, is known as a strong proponent of IFRS. And over 100 countries had either required or permitted publicly traded companies to report under IFRS by the end of 2008, with more scheduled to come on board by the end of 2011. In the US, foreign private issuers can already report under IFRS without having to reconcile their reporting to US GAAP (Generally Accepted Accounting Principles), and many companies that don't trade on US exchanges are already IFRS compliant.

Even if the US postpones the issue, IFRS is still an important accounting standard for stakeholders in the global economy. It also has implications for stakeholders in US companies, especially given the ongoing efforts of the US-based FASB (Financial Accounting Standards Board, the overseer of US GAAP) and the IASB (International Accounting Standards Board, the standard-setter for IFRS) to converge the two accounting standards.

From a philosophical standpoint, at the heart of the debate over IFRS adoption is the question of whether a global accounting standard is either feasible or desirable. Politically, IFRS is entangled in a change of administration in the US and the inevitable tug of war between corporations and standard setters over specific rules promulgated by the IASB. Economically speaking, the important issues involve tax questions, the costs involved in a transition to IFRS, and whether a global accounting standard will ultimately be more transparent and more valuable to investors and stakeholders.

Any mandate that would force publicly traded companies to adopt IFRS has implications far beyond technical accounting issues—the shift would virtually affect a company's entire operation. Investors need to get a handle on what the impact will be, how particular companies will handle the transition, and how their IFRS financial statements will diverge from their US GAAP statements.

"You'll see operational, technological, tax, human resources, compensation, revenue, and many other changes in an IFRS transition," says Amy Edwards, senior manager at Ernst & Young's on-call advisory services practice. "At the beginning it's about the accounting, but it becomes a businesswide project with all the different aspects of the business having to work together to figure out how to come up with an IFRS transition plan that makes sense for the entire company."

AN IFRS PRIMER

IFRS is a body of accounting standards created by the IASB, an independent standard-setting body that is part of the IASC (International Accounting Standards Committee) Foundation. The IASC Foundation is a private nonprofit funded by donations from corporations, associations, central banks, international organizations, international accounting firms, stock exchanges, and levies on corporations by national securities regulators.

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Current Major Differences between IFRS and US GAAP

	US GAAP	IFRS	Impact
Inventory Valuation	Permits LIFO, FIFO, weighted average cost, or specific identification. Inventory carried at lower of cost or market.	Permits FIFO or weighted average cost; LIFO not permitted. Inventory carried at lower of cost or net realizable value.	Companies that use LIFO must revalue inventory, which could result in major tax liabilities due to the IRS's LIFO conformity rule.
Asset Impairment	Two-step impairment.	Single-step impairment.	Write-downs are more likely under IFRS.
Asset Valuation	Assets can be written down, but not written up. PP&E is valued at historical cost.	Allows upward revaluation when an active market exists for intangibles; allows revaluation of PP&E to fair value.	Book values are likely to increase under IFRS.
Revenue Recognition	Provides very specific general and industry guidance about what constitutes revenue, how revenue should be measured, and the effect of timing on recognition.	Not specific about the timing and measurement of recognition; lacks industry-specific guidance.	Revenues are likely to increase with less detailed guidance.
Contingencies	Contingent liabilities must be disclosed.	Can limit disclosure of contingent liabilities if severely prejudicial to an entity's position.	May result in fewer disclosures.
Debt Covenants	Permits curing debt covenant violations after fiscal year end.	Debt covenant violations must be cured by fiscal year end.	Debt covenants may need to be amended, resulting in related transaction costs.
Research & Development	R&D costs must be expensed.	Allows capitalization of R&D costs.	Development costs will be deferred and amortized.
Entity Consolidation	Consolidation is based on who has the controlling financial interest.	Consolidation is based on which entity has the power to control.	Companies are likely to consolidate more entities.
Securitization	Allows certain securitized assets and liabilities to remain off a corporation's books.	IFRS requires most securitized assets and liabilities to be placed on the balance sheet.	May result in very different balance sheet values.
Financial Instrument Valuation	Fair value based on a negotiated price between a willing buyer and seller; not based on entry price.	Several fair value measurements. Fair value generally seen as the price at which an asset could be exchanged.	Financial assets and liabilities will be measured differently.
Depreciation	Methods allowed: straight-line, units of production, or accelerated methods (sum of digits or declining balance). Component depreciation allowed but not commonly used.	Allows straight-line, units of production, and both accelerated methods. Component depreciation required when asset components have different benefit patterns.	Assets with different components will have differing depreciation schedules, which may increase or decrease assets and revenue.

Sources: American Institute of Certified Public Accountants, Ernst & Young, and Deloitte Touche.
Terminology: LIFO (last in, first out), FIFO (first in, first out), PP&E (property, plant, and equipment).

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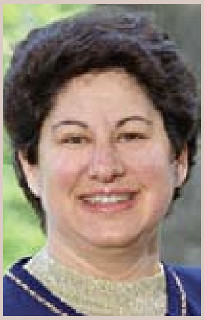
Amy Edwards, senior manager at the on-call advisory services practice of Ernst & Young's New York financial services office

- Specializes in asset management issues, with a special focus on FAS 157 and IFRS
- Served as the controller of a $10 billion hedge fund

"From an analyst's standpoint, what is really going to be interesting is that, if this does happen in the SEC's projected timeframe, you're really going to have to understand US GAAP and IFRS at the same time and really be able to quantify those differences. There are going to be a couple of years when you are going to have to look at companies in the same industry, some of which are using GAAP and some of which are using IFRS, and understand why they have different earnings, why they have different ratios or different capital, until everyone is on the same page."



Suzanne Hoffman, vice president of worldwide sales at Star Analytics

- Holds a certificate in management from the University of Chicago's Graduate School of Business
- Frequently gives seminars on business intelligence technologies and XBRL (eXtensible Business Reporting Language)

"There is no doubt that this issue is the 'quiet giant' with far-reaching implications for securities analysts, finance departments, and investors. Given the current economic situation, it's important to look at standards like IFRS in the context of the critical state of antiquated corporate finance systems for reporting and consolidation."

Rudolph Jacob, PhD, professor of accounting and chair of the accounting department at Pace University

- Former faculty fellow at Coopers & Lybrand
- Research interests include financial, managerial, and international accounting issues

"Since IFRS is more principles-based than US GAAP, it allows for much more judgment in capturing the economic substance of a transaction. Preparers, auditors, and securities analysts will have to undergo a significant mindset change if the US adopts IFRS."

The foundation was created to develop a single set of high-quality, transparent, comprehensible financial reporting standards that corporations around the globe could employ to produce their financial statements. Since the IASB was founded in 2001, more than 160 countries have either mandated or permitted the use of IFRS by publicly traded companies or are in the process of adopting these standards. In 2006, the FASB and IASB collaborated on an MOU (memorandum of understanding) that outlined how the two organizations planned to approach the convergence of US GAAP and IFRS.

The initial creation of IFRS, the development of the MOU between the IASB and FASB, and the SEC's proposal that US publicly traded companies adopt IFRS in place of US GAAP—that all springs from the promise that one widely adopted international accounting standard will serve the public interest, promote transparency and understanding for stakeholders, and allow capital to move more freely across national borders.

To this end, the IASB is working to improve IFRS and is cooperating with the FASB to eliminate the differences between IFRS and US GAAP. "This move is really about investors and providing a common accounting language and high-quality global financial information," says Linda MacDonald, CPA, a senior managing director of the forensic and litigation consulting segment at FTI Consulting. "My view is that it is the best thing for the investors. I support the FASB and IASB continuing to work together to make improvements in IFRS, to converge IFRS and US GAAP, and, at that point, to have the US move over to IFRS."

While the convergence process has made some progress, there is still a long way to go. Many significant differences continue to divide the two accounting standards. The US approach to accounting standards is more rules-based than that of other countries, due to the unique legal, regulatory, and enforcement systems here, says Peter Bible, CPA, partner in charge at the public companies group of Amper, Politziner & Mattia.

"In the rules-based structure we have now, the objective is that there is or will be a rule for literally every transaction. The intent is to limit the use of judgment," he adds. "In applying accounting standards in the US we have almost what you would call a cookbook approach to accounting, whereas international standards are principles-based, which means there are broad, sweeping principles that allow or actually require the use of judgment."

Patrick Daugherty, JD, attorney and chief strategy partner with the business law department at Foley & Lardner, agrees. "The FASB has become like the IRS in promulgating rules for everything, creating a very rules-heavy accounting system. In terms of the difference between where the US is now and IFRS, you need to think pre-Sarbanes–Oxley in terms of financial statement rigor. Or even back further, say 20 years or so. That's IFRS. That means it will be harder to make straight-up comparisons of companies in the same industry."

This could mean that corporate accountants and chief financial officers will have to be forthcoming about the decisions and judgment calls they make in applying IFRS rules to their books and their financial statements. Companies in individual industries may

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need to work together to treat certain issues the same way, to make comparability across industries uniform.

It could also bring less transparency and less comparability to financial statements as corporate accountants apply judgment, resulting in very different outcomes even in similar situations. IFRS has been criticized for allowing too much judgment in crucial areas such as revenue recognition, which directly impacts corporate earnings. "Earnings are much more subject to manipulation under IFRS than US GAAP," says Tom Selling, CPA, PhD, a retired accounting professor and author of the Accounting Onion blog. "And the SEC will have a lot less power to enforce rules because there will be fewer rules and they won't be in charge."

PHILOSOPHICAL ISSUES AT STAKE

While the Big Four public accounting firms are major proponents of a transition to IFRS, not everyone is convinced that one global accounting standard is even possible, much less advisable. Even some tentative supporters of the transition don't concede that we're ready for the change to transpire quite yet.

"An ultimate switch to one standard is a good idea," says Jack Ciesielski, CFA, CPA, publisher of the Analyst's Accounting Observer. "There should be one set of standards if economics means the same thing to all people. But I would much prefer to see the situation stay where it is now and have the FASB and IASB continue to work on convergence to the point where nobody knows whether they are using an FASB or an IASB standard because they are so similar. And that could take 15 to 20 years."

Others disagree that one international standard is the correct approach. "Alternative systems should always exist," says Selling. "There is a benefit in not being standardized in accounting, in a situation that combines a level of cooperation between standards with a level of departure involving fundamental differences."

He continues, "I hate to say it this way, but it's almost like fascism. The principle behind fascism is that there is only one game in town and it's good for everyone." Selling and others believe that accounting standards benefit from competition in a marketplace of ideas and that the best ideas aren't likely to come to the fore if only one standard exists.

No clear indication has emerged from academic studies as to which standard is superior, says Rudolph Jacob, PhD, chairman of the accounting department at Pace University. "The results, the empirical studies in this area are very mixed. It's not even clear how to measure the differences," he confesses.

That ambiguity is why some argue in favor of keeping both standards and perhaps even allowing US companies to select a standard to employ. "Investors are going to choose which standard they prefer to use," Jacob says. "In a sense, this would allow the free marketplace to decide whether IFRS or US GAAP is better. Investors will ultimately prefer the standard that provides the most useful information in evaluating investments."

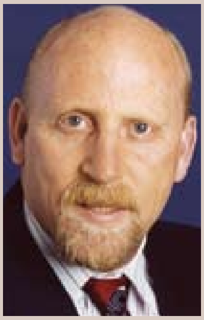
Shyan Sunder, PhD, the James L. Frank Professor of Accounting, Economics, and Finance at the Yale University School of Management, believes that the goal of promoting uniformity and conformity

Linda MacDonald, CPA, senior managing director in FTI Consulting's forensic and litigation consulting division

- Served as a director at the FASB
- Served as a staff member at the SEC Division of Enforcement

MARC LOONAN

"There are more than a hundred countries now that permit or require IFRS. The IASB is certainly in position to become the global standard setter, but in terms of understanding the move and opining on the timing, I think it's important to keep in mind that both IFRS and US GAAP need improvement through the ongoing convergence efforts in process by the Boards."



Paul Munter, CPA, PhD, partner in the department of professional practice, audit and advisory services, KPMG

- Participated in the SEC's IFRS roundtable, August 2008
- Served as the academic fellow in the office of the chief accountant at the SEC
- Former KPMG professor and chairman of the department of accounting at the University of Miami, Coral Gables, Florida

"Ultimately, analysts should be as well-versed in IFRS financial statements as they are in US GAAP reporting. They will need to understand the nuances of IFRS in order to make appropriate investment decisions and recommendations. Investors will ultimately utilize reports from those analysts whose information is the most complete. Additionally, since foreign private issuers already can use IFRS and many do, there are a number of significant investment alternatives currently available to US investors reporting under IFRS."

Vincent Papa, CFA, senior policy analyst at the CFA Institute Centre for Financial Market Integrity in London

- Serves on the IASB's Analyst Representative Group
- Completing a doctoral thesis in derivative accounting and earnings management through the Cranfield School of Management
- Master's degree in finance from London Business School

"It is very simplistic when people say that IFRS is all principles-based, versus US GAAP, which is rules-based. You really need to look at it on a standard-by-standard basis. You really need to look across the spectrum of standards and understand what that means across different countries."

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through global adoption of IFRS is unobtainable. "IFRS will bring about neither uniformity nor comparability in any meaningful way," he argues. "The idea that you can apply a given set of rules across the world and get comparable results is actually nonsensical."

He explains, "Even in various industries within different countries, accounting rules differ. It has often been argued that you cannot use the same rules for, say, the utilities industry and the software industry. So if you can't use the same rules across industries in a given country, imagine applying the same rules across 200-plus countries around the world and getting the same results."

In fact, there is already significant divergence in the ways in which countries that have mandated or will soon mandate IFRS actually apply the standard. Many countries "carve out" areas in which they apply their own standards that are distinct from IFRS, often in response to political pressures.

"Special interests are trying to shape the way the standards are coming through, and that creates problems," says Vincent Papa, CFA, senior policy analyst with the CFA Institute Centre for Financial Market Integrity in London. "In the UK, the banking sector is a huge part of the economy and the bankers have much more leverage with the politicians than they do in the US. If the accounting is not friendly to their requirements they can wield influence to change it."

If a number of countries reserve areas where local standards prevail over IFRS, a true international accounting standard won't exist, because there will be so many exceptions. Selling gives the example of China, which is working toward IFRS conversion, but is looking at carving out an exception to IFRS for related party transactions.

"The Chinese have a real problem with related party transaction disclosures. They don't want to disclose when the government, which controls a lot of the entities over there, enters into transactions that disadvantage the entity in favor of the government," Selling says. "They may not be doing that now but they want to have the license to do it, and there is nothing transparent about it."

DOMESTIC DISPUTES

Multiple domestic issues specific to the US surround the potential adoption of IFRS, from the new presidential administration, to the role of the FASB and the SEC, to the motives of opponents and proponents.

After the SEC's roundtable conference in August 2008, a roadmap for the IFRS transition was expected. However, the release of that roadmap, originally scheduled for a few weeks after the roundtable, was delayed significantly—in fact, it wasn't issued until just after the presidential election in November. Some people find that chronology suspicious, alleging that Christopher Cox was attempting to pressure the Obama administration into following his agenda, and that he sees the adoption of IFRS as an important part of his political legacy. Others blame the financial crisis that has forced the government to take a central role in bailing out the banking system to restore a functioning lending market.

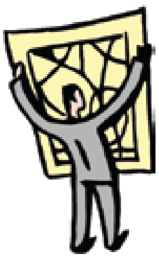
In the roadmap, the SEC has proposed that approximately 110 publicly traded companies that are large accelerated filers be

SEC encourages the international community to work toward IFRS.

1988

1997

SEC notes that multinational companies filing in multiple countries face increased compliance costs and accounting requirements due to lack of IFRS.



IASB is established to work on IFRS.

2001

Agreement between IASB and FASB to work toward convergence.

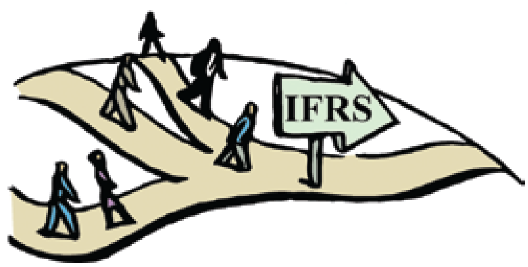
EU sets 2005 timeline for IFRS compliance.

2002

2005

SEC releases roadmap to allow foreign companies to file without US GAAP reconciliation by 2009 or sooner.

Publicly traded companies in 92 countries, including EU members, migrate to IFRS.



IASB and FASB declare their intention to work together on major projects aimed at accounting standards convergence.

SEC chairman Christopher Cox reaffirms his support for one set of high-quality global accounting standards.

2006

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allowed to report under IFRS on a voluntary basis beginning at the end of 2008. In 2011, the SEC will assess several factors—including IFRS education and training efforts in the US, improvements in IFRS, and funding and accountability of the IASB—to decide whether to require mandatory adoption of IFRS.

If the SEC decides to go ahead with the mandate, large accelerated filers would be required to issue three years of IFRS financial statements for fiscal years beginning on December 15, 2014, or later. For accelerated filers that start date would be December 15, 2015; and for nonaccelerated filers, December 15, 2016. Large accelerated filers that decide to adopt IFRS voluntarily before the end of 2014 would first need to obtain a letter of nonobjection from the SEC.

As to whether companies that have the option to convert early would in fact do so, Paul Munter, CPA, PhD, a partner in the audit and advisory department of professional practice at KPMG, says, "Companies that are eligible for early adoption under the SEC proposal should analyze whether they would gain an advantage by being an early adopter or waiting. The decision depends on a variety of factors."

He explains, "The larger the global footprint, the greater the motivation to convert early, especially if more of their subsidiary operations have statutory reporting utilizing IFRS. If more of their industry peers are using IFRS, converting to IFRS would offer the benefit of greater comparability in financial reporting with those peers."

Ciesielski believes that few large accelerated filers would choose to go with IFRS in the absence of a mandate, pointing out that the lack of clear-cut benefits would deter companies from making a change that is likely to be expensive and might not be permanent. He's also critical of the roadmap, asserting that it's unrealistic, given the complex issues surrounding convergence that still need to be hammered out by the IASB and FASB.

"The path we've been on is one of gradual evolution, it's been the IASB working with the FASB to get joint standards. This is not a process that can work by decree. And when you see in the third MOU between the FASB and the IASB what they expect to accomplish by 2011, you see that we don't have to worry about this thing because it ain't going to happen—it's like the moon shot happening in one week instead of a decade."

Another domestic issue is the role of the FASB during the transition period. In a comment issued before the SEC published the roadmap, MacDonald opined that although that role is still fairly malleable, one possible scenario would be for the FASB to remain in existence as a component of the IASB. "The IASB is headquartered in London, so down the road, depending on how the transition moved, the IASB might find it useful to have a presence in the US through the FASB organization, in order to help liaison with its US constituents," she says.

A second possibility is that the FASB would remain in existence after the transition of publicly traded companies to IFRS, and would continue to set accounting standards for privately held companies and nonprofits, as their status is unclear in any potential move to IFRS. In this scenario, the FASB could also act as an advocate before the IASB on behalf of US publicly traded companies and US accounting interests.

2007

SEC allows foreign private issuers to report using IFRS, dropping the GAAP reconciliation requirement.

Brazil, Canada, Chile, Japan, India, and Korea adopt IFRS convergence timelines.

2008

SEC holds roundtable, solicits comments, and issues a proposal regarding US transition to IFRS.

2009

The extended comment period ends and the SEC is likely to rule on whether to proceed with its IFRS transition proposal.

If proposed changes hold, certain US large accelerated filers may begin to use IFRS.

Chile and Korea to move to IFRS.

2011

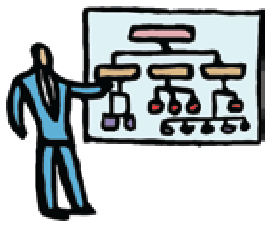
SEC expects to examine IFRS standards, structure, and funding, and the progress of adoption to date.

SEC likely to allow US companies the option of filing under IFRS.

India and Canada to complete move to IFRS; Japan and China to finalize convergence between local GAAP and IFRS.

2014

Large accelerated filers may have to transition to IFRS.

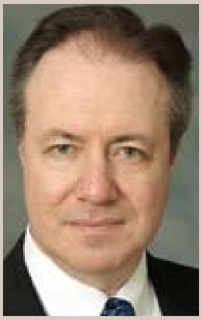


2015

Accelerated filers may have to transition to IFRS.

2016

Nonaccelerated filers may have to transition to IFRS, completing the changeover from US GAAP for all US publicly traded companies.



Bruce Pounder, CFM, CMA, president of Leveraged Logic

- Author of *The Convergence Guidebook for Corporate Financial Reporting* (Wiley 2009)
- Earned the Johnson & Johnson Gold Medal for achieving the highest score in the world on the examination to attain the certified financial manager designation in 2004
- Earned a diploma in international financial reporting from the Association of Chartered Certified Accountants

"There is the potential for countries to introduce idiosyncratic differences in IFRS, and the risk is that we end up right back where we started, where every country has its own standards. It's completely, completely the antithesis of the whole idea of us having one country-neutral global set of standards."

Tom Selling, CPA, PhD, professor emeritus, Thunderbird School of Global Management

- Author of the Accounting Onion blog
- Former academic fellow in the office of the chief accountant at the SEC
- Coauthor of *International Financial Reporting and Analysis* (McGraw-Hill/Irwin 1999)

"Is a true international accounting language achievable? I don't think anyone thinks so. Everyone thinks there is going to be a carve-out for different countries on different issues. Every country has different policy objectives for their accounting standards, so it is hard to see how one set of standards will fit everyone."

But having a dual financial standards reporting system in place in the US for years could create major confusion for investors. Imagine the largest publicly traded companies using IFRS, midsize publicly traded companies transitioning from US GAAP to IFRS, smaller publicly traded companies that have not yet begun to transition, and investment companies and privately held companies that aren't on board at all.

Still, IFRS does have its supporters. The Big Four accounting firms, the AICPA (American Institute of Certified Public Accountants), and many CPAs are in favor of IFRS. Members of the accounting community, especially the Big Four, have a large stake in IFRS adoption because they are positioned to provide the training and consulting services that US companies will need. Sunder speculates that these firms may see a transition to IFRS as a chance to squeeze out smaller rivals.

Many US GAAP supporters, on the other hand, have an interest in keeping the current structure in place. US standard setters, politicians, regulators, and other US GAAP stakeholders wouldn't have as much influence over an international standard as they do over a domestic one. Selling sees a role for accounting professors as an unbiased source of information about the potential advantages and disadvantages of a switch to IFRS. "I think one of the problems with this IFRS issue is that there are not a lot of people out there who can set aside their personal payoff in this whole thing and contribute to the debate," he says.

MONEY TALKS

Internationally, the IASB has been accused of caving in to political pressure to alter previously established standards. Critics charge that the IASC Foundation's voluntary funding mechanism makes it too vulnerable to corporate and political lobbying and that the absence of an international regulator to back up the IASB's rules will make enforcement impossible.

Donna Street, PhD, who holds the Al and Marcie Mahrt Chair in Accounting at the University of Dayton, asserts that the IASB's independence is crucial to the future functionality of a global accounting system. "The IASB is funded by voluntary contributions that in the past haven't been very diverse. Substantial portions of the funding come from the Big Four accounting firms," she says. "How you come up with a funding structure for a global body like that is going to be very, very difficult." Flawed funding mechanisms could compromise the integrity of the IASB because financial contributors could wield too much influence over the composition of the board members.

Street is also concerned about the formation of a new monitoring group comprised of securities authorities that include "the responsible member" of the European Commission and the SEC chairman. She fears that allowing the monitoring group to approve trustee positions could result in trustee and IASB appointments that stem from political expediency, rather than technical competence, threatening the objectivity of the emerging standard.

"The political issues that the IASB has been dealing with over the past several months, including changing the classification rules for financial instruments, may make IFRS less desirable for prospective adopters such as the US," says Papa. "The whole idea behind IFRS is to have an independent standard setter. When that is brought into question, it could significantly impact adoption."

ECONOMIC FALLOUT

Corporate CFOs who are paying attention to the IFRS debate are concerned about the potential cost of a switch to IFRS. The SEC attempted to quantify that cost in its IFRS proposed-rule release, estimating that corporations could expect to spend between 0.125% to 0.13% of annual revenue on IFRS conversion. Ciesielski believes these estimates are "incredibly below" what actual costs are likely to be, given that Sarbanes–Oxley was much more expensive and complicated to implement than the SEC anticipated, and that a

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switch to IFRS will dwarf the Sarbanes–Oxley implementation process in complexity.

As Edwards notes, a transition is likely to affect all aspects of a corporation's business and the analysts covering that company will have to understand the potential impacts. One major area of expense is likely to be in technology and training, as companies replace old systems with new systems that are capable of running IFRS and US GAAP side by side during the transition. "Laying the right technology foundation allows companies to adapt early as these new standards evolve, and to avert what could potentially be one of the most substantial upheavals we've seen in financial reporting in decades," says Suzanne Hoffman, vice president of worldwide sales for Star Analytics.

Unfortunately, many inattentive CFOs may be in for a rude awakening should the SEC move forward in 2009 and 2011 with IFRS implementation. Bruce Pounder, CFM, CMA, author of *The Convergence Guidebook for Corporate Financial Reporting*, explains, "Because of inertia and the unfolding financial crisis, many companies aren't paying attention to IFRS. IFRS is strange. It's foreign. If you're not familiar with something and you're really busy, your first response will be to ignore it until the shareholders and securities analysts start calling, asking what you're going to do. And you probably won't have good answers at that point."

Pounder believes that, when the time comes, companies that put off transitioning to IFRS risk losing competitive advantages to the companies that do make the switch and to those overseas businesses that already switched some time ago. These advantages include access to global capital and access to international accounting and finance talent.

"Looking at what was discovered in the UK, we see that certain companies that operate in an environment very similar to the US experienced a significant reduction in their cost of equity capital as a result of switching to IFRS," he says. "From a strategic finance point of view, if all else is equal, if your competitor has a lower cost of equity capital, if they can get capital more cheaply than you, they have a huge competitive advantage over you."

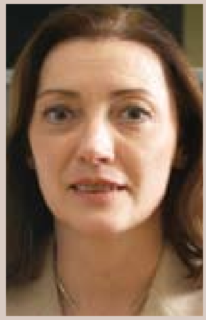
Selling disagrees, saying, "That's a bunch of hooey. The capital is in the United States." He believes that the potential disadvantages far outweigh the potential advantages—disadvantages that include the current major differences between IFRS and US GAAP; the obscuring of comparability and, in some cases, transparency; and the significant costs likely to be involved in any transition.

THE BOTTOM LINE

The debate is only just beginning. Whether or not the SEC adheres to its roadmap under new leadership, the IASB and FASB will continue their work on convergence, overseas companies will continue to convert to IFRS as their regulators move toward their own versions of convergence, and foreign private issuers will continue to report under IFRS in the US.

There is a possibility that the SEC will adopt its proposed rule sometime in 2009 and will formally move forward in 2011. The rule is available at www.sec.gov/rules/proposed/2008/33-8982.pdf. In addition, the SEC is actively soliciting comments from stakeholders in the process. Comments are due by February 19, 2009; a link to the comment form can be found on the SEC website at www.sec.gov/spotlight/ifrsroadmap.htm.

"If you don't pay attention and speak up now and say what you think, you're going to be living with things in a few years that will make you wonder how this all happened," says Ciesielski. "There are lots of nuances in this thing that are going to cause dislocations. I have to say, take a look at this and see if you can live with some of this stuff. Because your life is going to change and you may not be happy with it. A switch to IFRS may not be something that can be reversed once it's underway, so the time to comment is now." ■



Donna Street, PhD, professor and Al and Marcie Mahrt Chair in Accounting at the University of Dayton

- Vice president of publications for the International Association for Accounting Education and Research
- Associate coeditor of the Institutional Perspectives section of the *Journal of International Financial Management and Accounting*
- Author of more than 100 research articles

"In Europe in 2002 the EC said, 'We're going to do it,' committing to move listed companies to IFRS in 2005. So at some point the SEC, with the support of Congress, has to say, 'We're going to do it,' and set a date. Once we get to that point, then I think we can make the conversion in a few years. It's not going to take forever. But the SEC has to make that decision and that seems to be the challenge right now."

Shyam Sunder, PhD, James L. Frank Professor of Accounting, Economics, and Finance at the Yale University School of Management

- Immediate past president of the American Accounting Association
- Author of six books and more than 150 papers
- World-renowned accounting theorist and experimental economist

"Even though IFRS is being sold in the US and across the world on the grounds of uniformity and comparability, there is no such thing. It will bring about neither uniformity nor comparability in any meaningful way."

Amy E. Buttell is a journalist working in Erie, Pennsylvania.