

Why global standards?

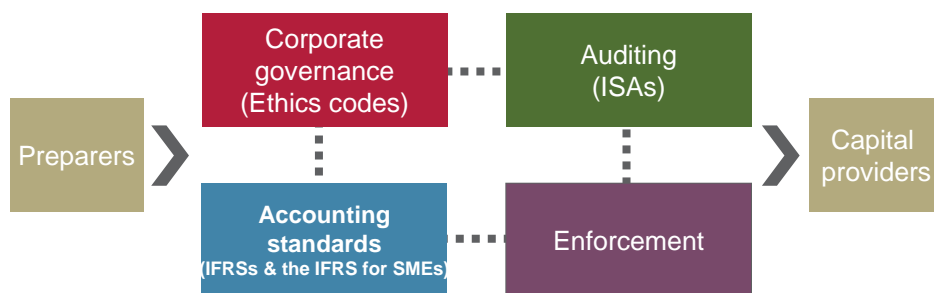
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Information supply chain

4



The reality

5

- Capital markets are global
 - New York, London, Luxemburg, Hong Kong, Singapore
- World's economies are interdependent
 - the financial crisis
 - SMEs integrated into the global economy
- Accounting and auditing needs strengthening
 - World Bank ROSCs
 - corporate failures
 - standard setters work programmes
- High-quality information facilitates the allocation of global capital

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Benefits of global standards

6

- Efficient allocation of capital globally
 - attracting investment through transparency
 - reducing the cost of capital
 - increasing world-wide investment
- Reducing costs and increased efficiency
 - facilitates standardising information systems
 - eliminates wasteful reconciliations
 - audit efficiencies
 - education and training

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The progress

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Status of IFRSs use around the world

8

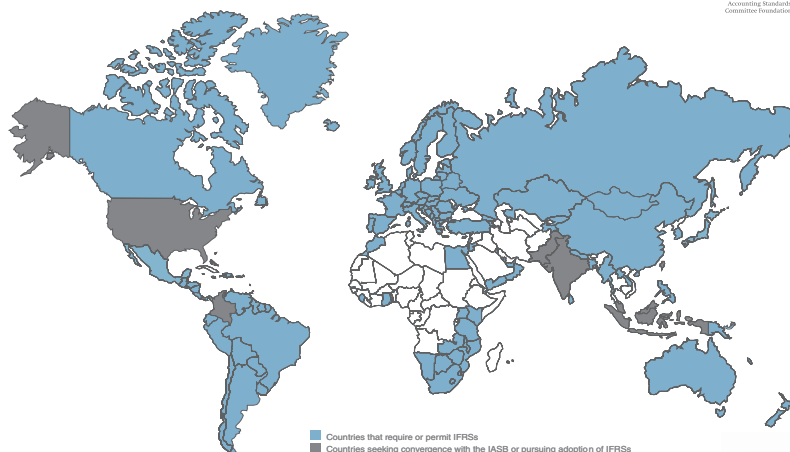
- Since 2001, over 120 countries have required or permitted the use of IFRSs.
- Remaining major economies have time lines to converge with or adopt IFRSs in the near future.
- Next wave of new joiners in 2011/2012: Argentina, Canada, Mexico, South Korea, etc
- Japan: IFRS permitted for a number of international companies since 2010; decision about mandatory adoption around 2012.



The World is Getting Smaller

9

THE MOMENTUM TOWARDS GLOBAL ADOPTION OF IFRSs
More than 100 countries require or permit the use of International Financial Reporting Standards (IFRSs), or are converging with the IASB's standards.



Source of information (adapted from): www.iasplus.com



Fortune Global 500 (July 2009)

10

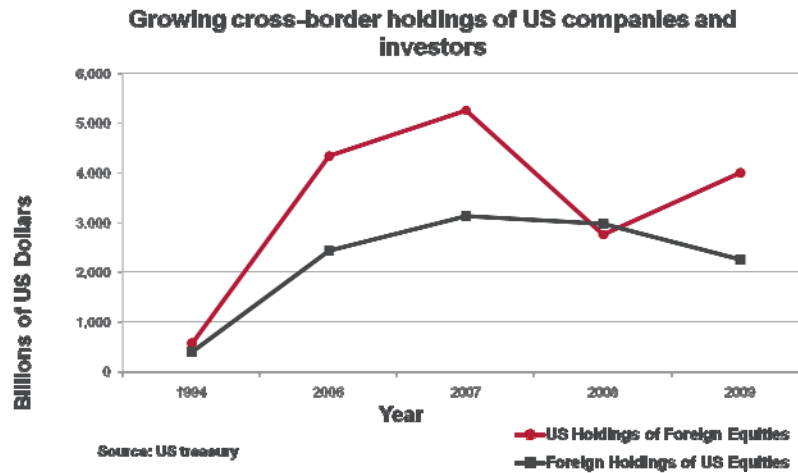
Fortune G500	Based on announced plans		
	2009	2013	Japan 2015?
Which GAAP?			
IFRSs and word-for-word IFRS equivalents	190	245	310
US GAAP	155	155	140
National GAAPs	155	100	50
Total	500	500	500

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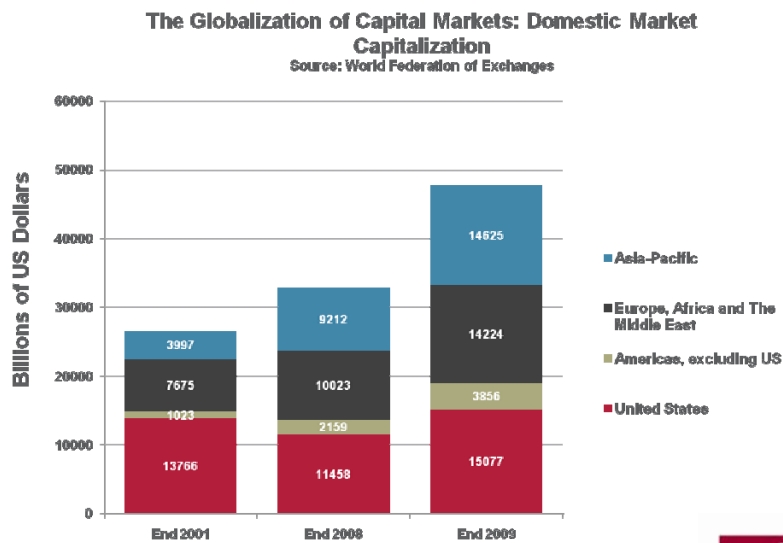
US investors, companies depend on cross-border capital flows

11



At the same time, US markets are diminishing in relative size

12



IFRS – FASB Convergence Process

13

2001 – 04	Reaction to investor desire for improved, global standards following Asian crisis and US financial scandals	IASB is established; enters Norwalk Agreement with FASB
2005 – 07	Growing IFRS adoption by major economies; continued US support and recognition of IFRSs as being high-quality standards	MoU accelerating convergence SEC removes reconciliation requirement
2008 - 09	Financial crisis; G20 pressure for convergence leading to adoption; focus on remaining major joint projects	Updates to MoU with 2011 targets and SEC roadmap
2010 - 2011	MoU timetable adjusted to ensure critical issues are completed.	Further SEC update to roadmap Modified convergence strategy prioritises major projects for June 2011 completion

G20 Summit – 25 September 2009

14

- Redouble efforts to:
 - achieve a single set of high quality, global accounting standards within the context of their independent standard setting process
 - complete convergence project by June 2011.
- IASB's institutional framework should further enhance the involvement of various stakeholders.
- G20 acknowledge that there could be differences between capital requirements and accounting rules:
 - to ensure comparability, the details of the leverage ratio will be harmonized internationally, fully adjusting for differences in accounting.

The importance of 2011

- IASB commitment remains
- A number of countries adopting or converging to IFRS around that time (2011/2012)
- G20 target date
- MoU target date
- US (2011) / Japan (2012) decision on adoption

However:

Primary focus: achieve significant improvements to financial reporting without compromising due process

Managing transition

- Limited effective dates: New requirements take effect either 1 January or 1 July of any given year
 - projects completed in 2010 not before 1 January 2012
 - projects completed in 2011 not mandatory before 1 January 2013
 - some even later
- Enhanced stakeholder engagement
 - improved and additional outreach activities
 - additional steps to engage with investors
 - enhanced technical dialogue with prudential supervisors and market regulators

Improved and additional outreach methods

- ✓ Enhanced investor engagement (among others dedicated Investor Relations Manager)
 - ✓ Enhanced outreach activities (project specific email alerts, pod casts of Board meetings, Feedback statements,..)
 - ✓ Enhanced technical dialogue
 - in line with G20 recommendations: proposals take account of guiding principles of Basel Committee and Financial Crisis Advisory Group report
 - regular meetings with the Basel Committee
 - member of the Financial Stability Board
 - regular meetings with EFRAG
 - national standard-setters are partners in our work
- participation in regional meetings of national standard-setters



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Modified strategy and work plan

Target date for priority projects remains June 2011

- Prioritise major projects to permit sharper focus on those areas in most urgent need for improvement in both IFRS and US GAAP
- Phasing of publication of EDs and related consultations to enable broad-based, effective stakeholder participation
- Publication of separate consultation document seeking stakeholder input about effective dates and transition methods



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The Major Projects

Crisis (MoU)

- Financial instruments
- Fair value measurement
- Consolidation
- Derecognition

Other (Non MoU)

- Insurance contracts

Other (MoU)

- Revenue recognition
- Leases
- Post-employment benefits
- Financial statement presentation
- Liability/Equity

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International Financial Reporting Standards

Structure and governance

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The vision

21

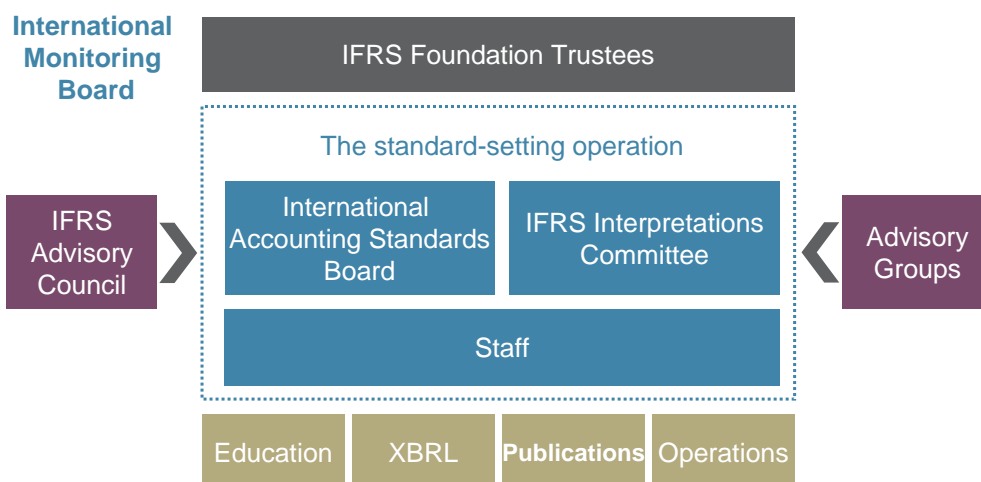
...one single set of high
quality global standards..

..used on the global
capital markets.



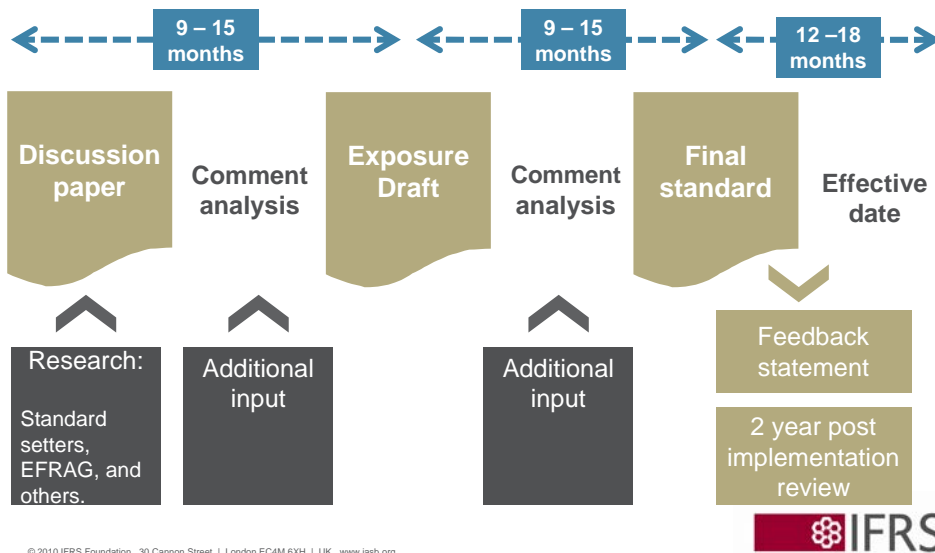
Structure of IFRS Foundation

22



Consultation process

23



Use of IFRSs – the ideal

24

Ideally, adopt IFRSs as the reporting framework:

- IFRSs as issued by the IASB in full
- Audit report and basis of presentation note refer to conformity with IFRSs
- Without local 'endorsement'

Use of IFRSs means all standards and all interpretations

- Sometimes the ideal is hard to achieve

Problems with local 'endorsement':

- Urge to tinker
- Time delay
- Politicisation
- Cost
- What does audit report refer to?
- If not IFRSs, will users understand?
- If carve-out, what is the replacement standard?



Understanding principle-based standards

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What does principle-based mean?

27

- There is overwhelming support for principle-based accounting standards
- But what does principle-based mean?
- In this presentation
 - an IFRS requirement is principle-based only when it is consistent with the concepts in the IASB's *Conceptual Framework*

What is *Framework*-based teaching?

28

In the context of IFRSs, *Framework*-based teaching relates the concepts in the IASB's *Conceptual Framework* to the particular IFRS requirements being taught

The IASB's *Conceptual Framework*

29

- *Framework* sets out **agreed concepts** that underlie IFRS financial reporting
 - the **objective** of general purpose financial reporting
 - qualitative characteristics
 - elements of financial statements
 - recognition
 - measurement
 - presentation and disclosure

Other concepts all flow from the objective



Role of the *Framework*

30

- IASB uses *Framework* to set standards
 - enhances consistency across standards
 - enhances consistency across time as Board members change
 - provides benchmark for judgments
- Preparers use *Framework* to develop accounting policies in the absence of specific standard
 - IAS 8 hierarchy

This presentation describes the role of the *Framework* in IFRS teaching



Objective of financial reporting

31

“Provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.”

Those decisions involve buying, selling or holding equity and debt instruments, and providing or settling loans or other forms of credit



Objective of financial reporting

32

- Primary users
 - provide resources, but cannot demand information
 - common information needs
- Assess the prospects for future net cash inflows
 - buy, sell, hold
 - efficient and effective use of resources



Fundamental qualitative characteristics

33

- Relevance
 - Predictive Value
 - Confirmatory Value
 - Materiality, entity-specific
- Faithful representation (replaces reliability)
 - Completeness
 - Neutrality
 - Free from error



Enhancing qualitative characteristics

34

- Comparability
- Verifiability
- Timeliness
- Understandability



Pervasive constraint

35

- Cost

- IASB assesses whether the benefits of reporting particular information are likely to justify the costs incurred to provide and use that information.

Note: It **is consistent** with the *Framework* for an IFRS requirement not to maximise the qualitative characteristics of financial information when the costs of doing so would exceed the benefits.



Elements

36

Asset

- resource controlled by the entity
- result of past event
- expected inflow of economic benefits

Liability

- present obligation
- arising from past event
- expected outflow of economic benefits

Equity = assets less liabilities

Income

- recognised increase in asset/decrease in liability in current reporting period
- that result in increased equity except...

Expense

- recognised decrease in asset/increase in liability in current reporting period
- that result in decreased equity except...



Recognition

37

- Accrual basis of accounting
 - recognise element (eg asset) when satisfy definition and recognition criteria
- Recognise item that meets element definition when
 - probable that benefits will flow to/from the entity
 - has cost or value that can measured reliably

What does probable mean?

Its meaning is determined at the standards level.

Therefore, inconsistent use across IFRSs 

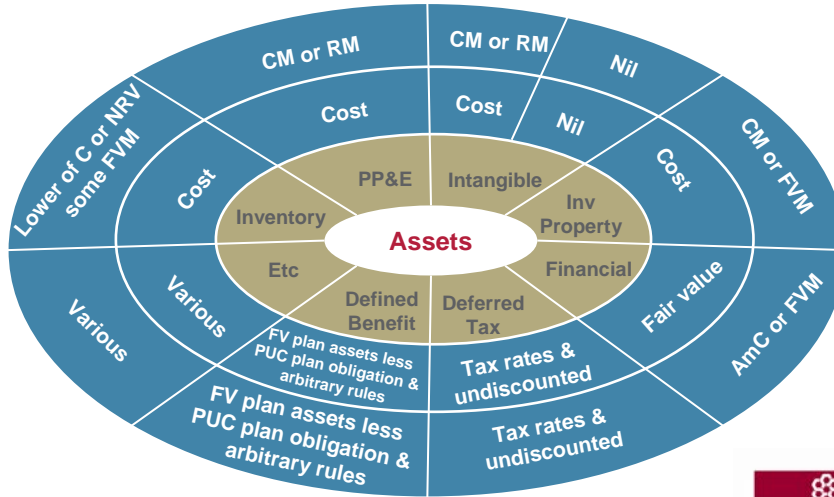
Measurement

38

- Measurement is the process of determining the monetary amounts at which the recognised elements are carried.
- IFRS measurements are largely based on estimates, judgements and models
- The measurement part of the *Framework* is weak and IASB has a project to replace it
- Measurement determined at the standards level. Therefore, inconsistent use across IFRS (see next 2 slides)

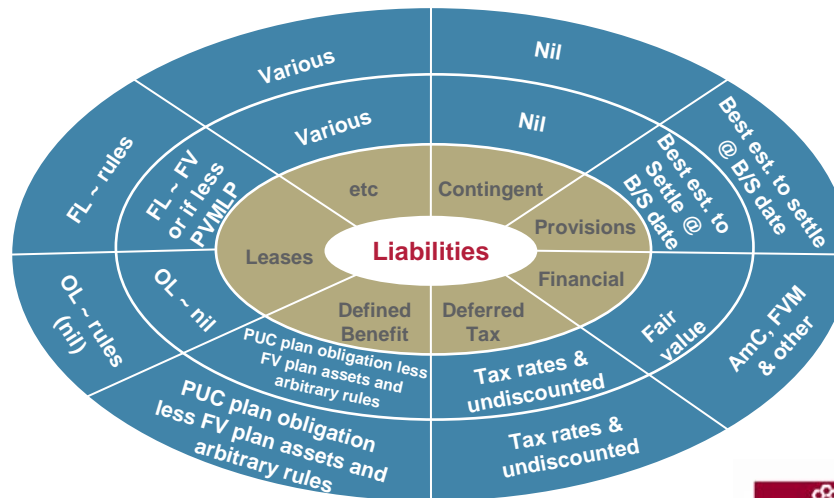
Asset

Classification, recognition and measurement



Liability

Classification, recognition and measurement



Framework-based teaching

41

- Because
 - the *Framework* sets out **agreed concepts** that underlie IFRS financial reporting, and
 - *Framework*-based teaching **relates the concepts** in the *Framework* to the particular IFRS requirements being taught

IFRS teachers should **first** teach their students

- the objective of general purpose financial reporting
- the concepts that flow from the objective
- which concepts are robust (and which are not)



Teaching suggestions—objective

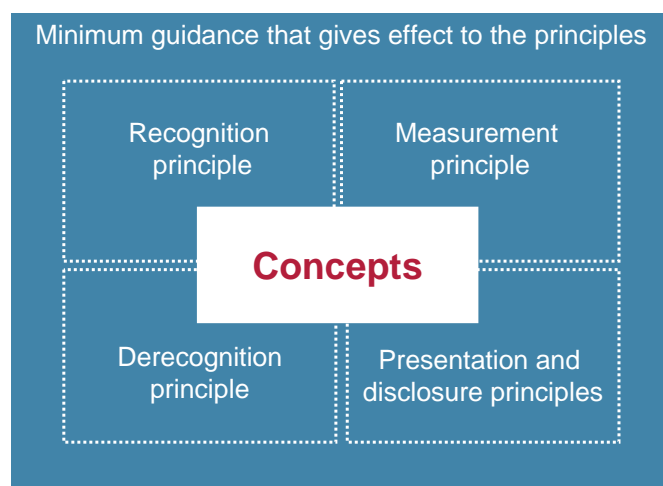
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- Contrast objective of IFRS financial statements with objectives of other financial statements
- Debunk myths
 - Myth 1: objective = record of historical costs
 - Myth 2: objective = support tax return
 - Myth 3: financial statements are designed to meet all the information needs of all users
- Before teaching the class the IFRS requirements for a transaction or event, discuss what information about that transaction or event would best meet the objective



Structure of a principle-based standard

43



The ideal principle-based standard

44

- Scope
 - no exceptions
- Principles
 - derived from the *Framework*
 - reliance on professional judgement to apply principles in business context
- Application guidance
 - explains application of principles

Get rule-based standards if

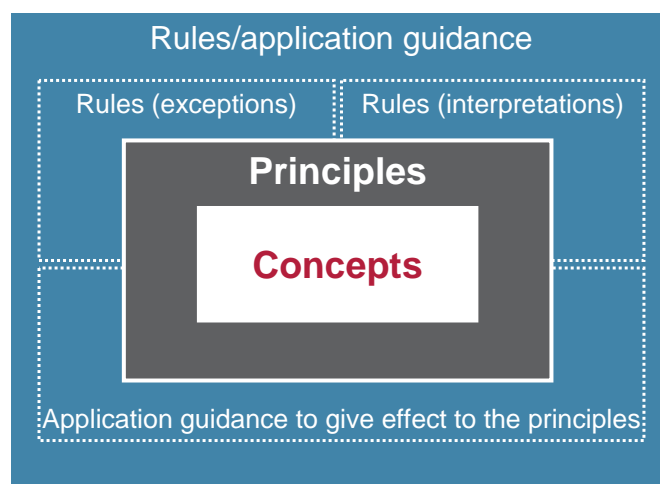
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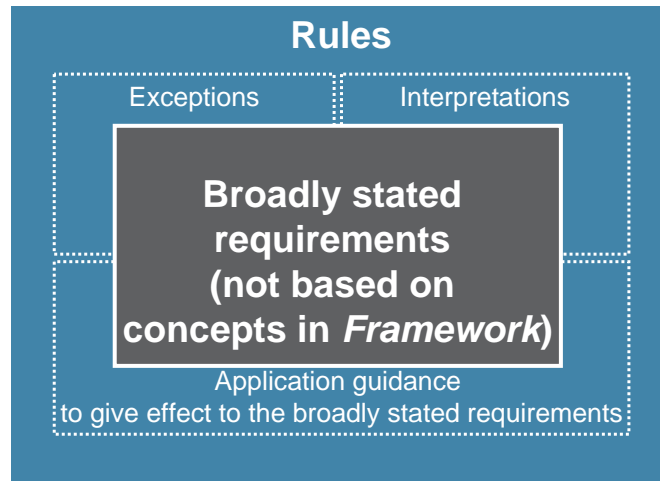
- Preparers and auditors
 - refuse to exercise professional judgement
 - don't act with integrity
 - ask for detailed interpretations
 - refuse to accept raw economic facts
- Regulators
 - want one answer in spite of different economic facts
- Courts
 - lawyers fail to defend reasonable judgements



Structure of some IFRSs

46





Framework-based teaching relates the concepts in the Framework to the particular IFRS requirements being taught

- Because the objective of the *Framework* is to facilitate the **consistent and logical formulation of IFRSs** *Framework-based teaching*
 - provides students with a cohesive understanding of IFRSs
 - prepares students to continuously update their IFRS knowledge and competencies

Framework-based IFRS teaching

49

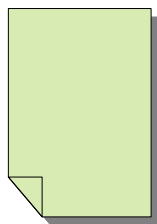
To a large extent, IFRS financial statements are based on estimates, judgements and models rather than exact depictions

- Because the *Framework* established the concepts that underlie those estimates, judgements and models it provides a basis for the use of judgement in resolving accounting issues
- By relating those concepts to the IFRS requirements
Framework-based teaching
 - enhances the ability of students to exercise the judgements that are necessary to apply IFRSs
 - prepares students to continuously update their IFRS knowledge and competencies



From concepts to principles to rules

50



Concepts



Principles



Rules



Examples 1a, b and c: Errors and changes in policies and estimates

51

- Objective
- Concepts
 - faithful representation
 - comparability
- Principle
 - **1a Prior period error**: retrospective restatement
 - **1b Change in policy**: retrospective application
 - **1c Change in estimate**: prospective application
- Rules
 - impracticable exception
 - specified disclosures



Examples 1a,b and c: continued

52

Teaching suggestions:

- build from objective to concepts to principles and rules
- explain how specified disclosures give effect to principle
- focus on judgements
 - eg differentiating changes in accounting estimates from changes in accounting policies and correction of prior period errors
- test understanding, eg use integrated case studies



What if requirement not principle-based

53

- When teaching the requirement
 - explain why IASB deviated from the main concepts in the *Framework* (see Basis for Conclusions (BfC). If no BfC then requirement could predate *Framework* (eg IAS 20))
 - discuss what a more principle-based requirement could be (consider rejected alternatives, subsequent IASB DPs and EDs, etc)
 - prepare students to continuously update their IFRS knowledge and competencies

A Guide through IFRSs cross-references all IFRS requirements to the Basis for Conclusions



Example 2: Lease classification

54

- Objective
- Concepts
 - faithful representation
 - element definitions
- Broadly stated lease classification requirement
 - capitalise in-substance purchases (finance leases)
 - other leases = executory contracts (operating leases)
 - is this requirement principle-based?
- Rules
 - guidance (eg contingent rentals)
 - specified disclosures



Example 2:
Lease classification continued

55

Teaching suggestions:

- explain broadly stated requirement is inconsistent with the *Framework* (see BfC ED *Leases*)
- discuss what a principle-based lease classification principle could be (eg see ED *Leases*)
- focus on judgements (eg use lease classification case studies)
- test understanding (eg use integrated case study)



Example 3:
Business combinations

56

- Objective
- Concepts
 - elements definitions
 - representational faithfulness
- Core principle
 - an acquirer of a business (scope)
 - recognises assets acquired and liabilities assumed (recognition principle)
 - at their acquisition-date fair values (measurement principle)
 - discloses information that enables users to evaluate the nature and financial effects of the acquisition (disclosure principle)



Example 3:
Business combinations continued

57

- Rules
 - exceptions to the recognition principle
 - exceptions to the measurement principle
 - specified disclosures

Example 3:
Business combinations continued

58

Teaching suggestions:

- build from objective through concepts to core principle and rules
- recognition—explain reason for removing
 - (i) the probability criterion; and
 - (ii) the explicit reliability of measurement criteria (see Basis for Conclusions on IFRS 3 paragraphs BC125–BC130)
- explain reasons for exceptions to IFRS 3:
 - recognition principle
 - measurement principle(see Basis for Conclusions on IFRS 3)

Example 3: Business combinations continued

59

Teaching suggestions (continued):

Focus on judgements, eg

- identifying a business, measuring fair value in the absence of an active market etc

Test understanding, eg:

- integrated case studies
- discuss with reference to the objective and QCs whether uncertainty should enter recognition or measurement (for business combinations and then extend the discussion to other transactions and elements)

Range of IFRS classes

60

Can I use *Framework*-based teaching in my IFRS class?

- Yes, the starting point for all IFRS teaching should be the objective of IFRS financial information and the concepts that flow logically from that objective
- However, the extent of IFRS requirements taught are likely to vary by course level and to suit the objectives of the course

Common misunderstandings

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Common misunderstandings

62

The <i>Framework</i> does not...	Clarification—the <i>Framework</i> includes
include a matching concept	accrual basis of accounting—recognise elements when satisfy definition and
include prudence/conservatism concept	recognition criteria neutrality concept
include an element other comprehensive income (or a concept for OCI)	only the following elements—asset, liability, equity, income and expense
mention management intent or business model	

Common misunderstandings continued

63

Misunderstanding	Clarification
Principles are necessarily less rigorous than rules	Rules are the tools of financial engineers
There are few judgements and estimates in cost-based measurements	Inventory, eg allocate joint costs and production overheads PP&E, eg costs to dismantle/restore site, useful life, residual value, depreciation method Provisions, eg uncertain timing and amount of expected future cash flows



International Financial Reporting Standards

IASB's active agenda

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The Major Projects

Project	ED issued	Completion
Derecognition	✓	✓ IFRS issued
Consolidation	✓	▪ Q1 2011
Financial statement presentation (OCI)	✓	▪ Q1 2011
Liability/Equity		
Fair value measurement	✓	▪ Q1 2011
Post-employment benefits	✓	▪ Q1 2011

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The Major Projects

Project	ED issued	Completion
Financial instruments	✓	▪ Q2 2011
Revenue recognition	✓	▪ Q2 2011
Leases	✓	▪ Q2 2011
Insurance	✓	▪ Q2 2011

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Questions or comments?

67

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