IFRS Foundation® Adoption Guide 2017

DRAFT

Introduction

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The policy decision

The policy decision outlines the jurisdictions' future framework for financial reporting.

You need to get this one right. Everything flows from the policy decision.

Adopting IFRS Standards (the Standards) is best done with careful planning, commitment and a complete understanding of the implications.

The International Accounting Standards Board (the Board) recommends that the first step towards adopting its Standards is to set out the future framework for financial reporting—the policy decision.

Recommendation 1—build consensus

Few jurisdictions have the power to mandate the adoption of the Standards. In most jurisdictions, the policy decision is reached through consensus and adherence to due process.

Building consensus requires a clear articulation of:

- why a jurisdiction should adopt the Standards;
- which companies should apply the Standards; and
- how the adoption process will proceed.

Recommendation 1A—identify *why* a jurisdiction should adopt the Standards

Whatever the policy decision, critics will emerge as the project evolves and ask, not unreasonably, 'why are we doing this?'. This question needs to be answered clearly when developing the policy decision.

For some jurisdictions, identifying why it should adopt the Standards is obvious. The jurisdiction may lack the resources to develop local standards. Alternatively, a jurisdiction may develop local standards but find that their financial reporting framework is not recognised in international markets.

For other jurisdictions, identifying why they should adopt the Standards is not obvious. They may have strong accountancy bodies and a professional history of standard-setting or individual groups may resist the inevitable costs of change.

Consequently, the 'why' question and its answer is different for every jurisdiction. Although most jurisdictions focus on the importance of recognition in international capital markets, the answer is often more dependent on subtle factors, such as:

(a) those jurisdictions that focus on the credibility of capital markets decide adopting the Standards helps to eliminate the 'country discount' that can arise from investors' uncertainty about local accounting standards;

(b) others see that the adoption of the Standards improves local companies' access to foreign capital markets or encourages foreign direct investment;

(c) some seek to minimise the costs borne by local companies that have subsidiaries in their jurisdiction that have adopted the Standards.

Recommendation 1B—decide *which* companies should apply Standards

Equally important to the 'why adopt the Standards' is the 'which' question. Although the Board has concluded the Standards are appropriate for all companies with public accountability (that is, companies listed on stock exchanges, banks, insurance companies, mutual organisations and similar organisations that accept funds from the public), it recognises that the decision to adopt the Standards is a sovereign decision, and that each jurisdiction can and should make the choice on the basis of its own circumstances.

In deciding the Standards companies should apply, the Board recommends that jurisdictions give consideration to the current accounting standards and regulatory framework. Where a jurisdiction has developed capital market and has previously adhered to local accounting standards, a move to the Standards may be less of a significant change compared to other jurisdictions. For example, where a jurisdiction has an emerging market and does not have local accounting standards, then moving to the Standards is a significant change.

Small and medium-sized companies that are not publicly accountable (although there may be a local requirement for audited financial statements) often find that the cost of understanding and complying with the Standards exceed the benefits and thus are better served by the *IFRS for SMEs* Standard. Jurisdictions might decide to adopt the Standards for public accountable entities and the *IFRS for SMEs* Standard for non-public accountable entities but permit an option for companies to apply the Standards.

The jurisdiction profiles outline the variety of approaches taken to adoption. Here are some examples:

[Table to be inserted]

Recommendation 1C—stay close to IFRS Standards

It is recommended that jurisdictions do not amend the Standards or the *IFRS for SMEs* Standard in response to calls from local constituents. This is because:

(a) every amendment diminishes the credibility of the assertion that the jurisdiction has, in fact, adopted the Standards. Adopting the Standards is difficult and complex. The rewards come from the credibility gained by local companies when they make the unreserved statement of compliance required by IAS 1 *Presentation of Financial Statements*.

(b) the need to explain why local standards are almost IFRS Standards, losses much of the benefit from full adoption.

There is an important exception to this recommendation. The Standards often include options, including the option for companies to adopt a new Standard before the mandatory date. This is particularly true today because some new Standards include long transition periods. The Board has long acknowledged that individual jurisdictions may decide to eliminate some of the options. A jurisdiction may decide, for example, that it is better for all companies to adopt a new Standard at the same time.

The Board is aware that some jurisdictions have adopted the *IFRS for SMEs* but have amended the standard for various reasons, including to incorporate a broader group of entities (such as not-for-profits or small financial institutions). Where this approach is adopted, the Board recommends that the *IFRS for SMEs* is adopted in full and that jurisdictions set out additional requirements in a separate local standard. This benefits the jurisdiction because it can assert compliance with the *IFRS for SMEs* while addressing local needs.

Recommendation 1D—explain how the adoption process will proceed

It is generally true that people do not like change, so it is important that jurisdictions are clear about how change is going to happen. In developing the policy decision, jurisdictions need to explain how the policy will be implemented.

Some jurisdictions adopt in a single 'big bang' step, while others follow a path of 'convergence' for a period before full adoption.

The big bang approach needs little description. A jurisdiction commits to adoption on a single date or, perhaps, a series of dates applied to companies of different sizes.

The convergence approach is a gradual move towards the Standards. This is a useful strategy when a jurisdiction needs to build professional capacity. Converging a few local standards to the Standards each year can allow local preparers and auditors to learn a few topics at a time rather than immersing themselves in the full set of the Standards. However, the following problems have been identified with a convergence approach and these should be taken into consideration:

(a) it is expensive—a convergence programme requires almost as much time, effort and cost as the creation of local accounting standards;

(b) it gives rise to complexity—often the local accounting standard and the Standards are not exact replacements, and jurisdictions need to make consequential amendments to local accounting standards;

(c) it does not eliminate the 'jurisdiction discount'; and

(d) it can create difficulties for users who, while getting used to the new Standard, also have to keep up with ongoing changes to the Standards, even though many of the changes are small; and

(e) it does not provide comparability from one year to the next: a jurisdiction that adopts a few of the Standards each year makes it difficult for users of financial statements to compare one year to the next.

Recommendation 1E—address copyright and a plan for translation now

Because the Standards are original standards created by the IFRS Foundation through its standard-setting body, the Board, the IFRS Foundation owns the worldwide copyright to the Standards in all languages and therefore owns the exclusive right to reproduce or authorise others to reproduce or translate the Standards. The IFRS Foundation offers a variety of different copyright agreements, each on the basis of the legal framework surrounding a jurisdiction's adoption strategy.

The IFRS Foundation recognises the central role of providing the Standards and supporting material in other languages. It therefore seeks the close co-operation of jurisdictions and organisations interested in producing translations of the Standards and related material. The translation of the Standards is an important component to consider when a jurisdiction prepares to make a policy decision to adopt the Standards

It is in the interest of any jurisdiction adopting or using the Standards or the *IFRS for SMEs* Standard that the translated standards are of a high quality. Countries adopting or permitting the use of the Standards will only be able to benefit from the comparability and transparency that the use of the Standards provides if they are rendered accurately and completely in each language.

For more information on copyright and translation, please refer to the *IFRS Foundation Translation, Adoption & Copyright Policy*: http://go.ifrs.org/TAC-Policy

Step two—the project plan

Nothing gets done without a plan

Recommendation 2—develop a project plan

Without a plan, the policy decision discussed in the previous section is an aspiration and has little chance of success. No company would build a factory, install new software or launch a new product without a plan. The same applies when adopting the Standards.

The successful adoption of the Standards requires a detailed project plan with clear objectives and milestones that establish accountability. Without objectives and milestones, there is a natural human tendency to defer and delay the project.

Many jurisdictions have published a project plan (often called a road map), complete with objectives and milestones, for the adoption of the Standards. Publication of the project plan helps establish accountability and identify obstacles that must be overcome.

Recommendation 2A—select a project lead

Somebody needs to be in charge and everybody needs to know who it is

Jurisdictions that have managed a successful adoption all seem to have identified a single organisation that drives the project. This should ideally be the statutory authority that has the responsibility to set accounting standards. Whatever organisation fills the role, all participants need to agree that this body is the team leader.

The Board has observed situations in which the leadership role is unclear. In some situations, no obvious leader exists or several organisations think that they are leading the project but none has the power to do so.

Recommendation 2B—form a committee

Everyone knows the popular criticisms of committees, and many are true. However, adoption is hard work; problems will arise.

Many jurisdictions that have successfully adopted the Standards have formed a committee (adoption committee) that monitors the project and addresses unexpected events as they arise.

Committee terms of reference

No matter how detailed the project plan, unexpected events always occur. Perhaps planners did not anticipate the effects of a Standard on a particular industry or the interaction with certain jurisdictional laws.

An adoption committee can monitor the project's progress and provide a means to address unexpected events and respond to them quickly. The monitoring process creates a loop and allows those in charge of the adoption plan to adapt and react.

The adoption committee should have authority to address problems and unexpected events but not to amend the Standards. The value of adopting the Standards comes from the fact that it is a single set of global standards. If every jurisdiction interprets the Standards in its own way, then it is inevitable that two jurisdictions will arrive at different answers to the same question.

The adoption committee terms of reference may include:

(a) monitoring the project plan;

(b) being a collection centre for identifying problems;

(c) being a distribution centre for sharing experiences, both local and international; and

(d) being an analysis centre for articulating problems and the characteristics of local law and business practice. That analysis is the first step in engaging people at the Board and others about problems encountered in the jurisdiction's adoption.

Committee members

An adoption committee should include the parties that are involved in setting the policy decision. Members of the committee can include:

(a) representatives of company organisations, because the companies are the ones who bear much of the costs of adoption. Company representative organisations can act as collecting agents for questions that the adoption may address.

(b) users of financial statements, because they know what they consider to be important in the financial statements of local companies;

(c) securities and prudential regulators, because they are the organisations that will enforce the application of the Standards;

(d) representatives of audit firms, because these firms see many companies and are often involved in helping to design a company's adoption plan. They have access to the firms' international networks and can utilise these networks for experience in other jurisdictions.

(e) the standard-setter (if they are not leading the project); and

(f) accounting bodies and accounting academics, because they will design the curriculum for upcoming generations of students and the training for accountants.

Recommendation 2B—identify issues in local legislation

The legal framework in most jurisdictions requires implementing legislation or regulation before a jurisdiction can adopt the Standards.

Jurisdiction profiles show a wide variety of implementing plans, ranging from incorporation by reference (so that each new Standard is automatically part of the local law and regulation) to endorsement processes that require specific actions by local officials. The policy decision should address details for implementing the Standards.

One of the important obstacles to IFRS Standards adoption often rests outside of the financial reporting community. In many jurisdictions, the most difficult and time-consuming task is often obtaining necessary changes in local company law.

For example, in one jurisdiction there are over 100 laws that refer to financial reporting and local accounting standards. The jurisdiction's legislative framework does not allow a single omnibus amendment to those laws. In another jurisdiction, only a single change was required. That change took several years to accomplish.

The Board does not have expertise in company law. However, it can share the experiences of other countries. Addressing local legal issues is an important part of building consensus. Legislators and makers of national policy rarely have expertise in accounting and financial reporting. They appropriately rely on the advice of those who are, and a consensus view can be persuasive.

Recommendation 2C—plan for IFRS 1

IFRS 1 *First-time Adoption of International Financial Reporting Standards* is the gateway Standard through which every jurisdiction must pass before its companies can make an unqualified statement of compliance with the Standards. This is true even if a jurisdiction's local accounting standards are identical to the Standards. IFRS 1 provides a mechanism to reboot the financial reporting system and a set of disclosures that explain the results of the change from local standards to the Standards.

Many question why companies in a jurisdiction should have the burden of applying IFRS 1. If the local standards are identical to Standards, what is the point?

Firstly, there are few situations in which local accounting standards are, in fact, identical. More often, the description 'identical except for' is more apt. One major difference can be found in transition provisions. Amounts reported in financial statements are path dependent.

Put more simply, history matters. If local accounting standards have different effective dates of transition, the amounts reported under those dates may be different from those that would result from following the Standards, even though the text of the standards is otherwise identical to IFRS Standards. IFRS 1 provides a means for dealing with differences in transition.

Secondly, IFRS 1 is designed to make the change to the Standards easier, not harder. It eliminates or reduces difficult measurement issues that companies would encounter in its absence.

Thirdly, the Board has shown that it is willing to consider amending IFRS 1 to meet local needs. We encourages adopting jurisdictions to share issues with us early in the process so that we can respond as necessary.

Step three—resources

Identify what you have and what you need

Recommendation 3—identify and plan resources

You have probably recognised that adopting the Standards is a resource-intensive exercise. Many of those resources are highly specialised and technical. This can be especially challenging in developing economies.

Recommendation 3A—identify local professional resources

Officials in many local jurisdictions are concerned that they lack the resources to adopt the Standards. Trained actuaries (pensions and insurance) and valuation specialists (financial instruments, investment properties, agriculture and business combinations) are often in short supply. The pool of available specialists may be shallow.

The problem is not as acute as it once was. As the Standards have gained worldwide acceptance, the number of local professionals who know and understand the Standards has grown.

This is true even in countries that have not adopted the Standards because local companies may have prepared IFRS-compliant financial statements for use in security offerings elsewhere. So, knowing what you have is the first step towards understanding what you need.

Recommendation 3B—build capacity

Capacity building is an issue for any jurisdiction that aims to participate in a global economy. Unfortunately, it is a problem for which the Board has a limited ability to help.

The Board has some resources that many jurisdictions have found helpful, but capacity building is an effort that demands continuous support. We will discuss that in Recommendation 3C.

Fortunately, there are other organisations that are active and can help. Those include:

(a) the World Bank;

(b) the International Monetary Fund;

(c) the United Nations Conference on Trade and Development;

(d) local and regional development banks;

(e) the regional standard-setting group; and

(f) professional and standard-setting bodies in valuation and actuarial practice.

The capacity needed to adopt the Standards is not limited to financial statement preparers and auditors. Securities and prudential regulators also need to address capacity needs.

Confidence in a jurisdiction's financial reporting system rests firstly on the standards that govern reporting and secondly on the perceived quality (regulatory) enforcement. The Board has protocols and working arrangements with Regulators and to support implementation.

Recommendation 3C—reach out to the Board

The Board's resources are limited, but it has several departments that are there to assist you. Those include:

The IASB Education Initiative

The Education Initiative's primary objective is reinforcing the IFRS Foundation's goal of promoting the adoption and implementation of the Standards. Consequently, a significant part of this effort is directed to countries that are in the process of adopting or that have recently adopted the Standards.

The Education Initiative's work includes organising conferences and workshops. These are often done in partnership with local bodies. A variety of organisations, including regional development banks and the World Bank's Centre for Financial Reporting Reform, can also provide support at local, regional or international levels.

Local technical workshops

Some jurisdictions have held successful local workshops that consider issues raised by practitioners. The goal is not to provide authoritative answers to questions but to explore the differing views and to consider how to move an issue forward. In some cases, consensus emerges from the discussion and no more needs to be done. In other cases, a local issue moves to the IFRS Interpretations Committee for discussion.

The Board may be able to provide speakers to support the workshop. More information can be found on the website in the speaking engagements section.

Technical queries

The Board does not operate a formal technical inquiry service. However, it has a long-established policy of responding to questions from local standard-setters, securities regulators, and bank and insurance regulators. Staff responses are not official positions of the Board, but they can help local officials who are trying to resolve questions.

The IFRS Interpretations Committee

The IFRS Interpretations Committee (the Interpretations Committee) is the interpretative body of the Board. It comprises 14 voting members appointed by the Trustees and drawn from a variety of countries and professional backgrounds.

The mandate of the Interpretations Committee is to review, on a timely basis, widespread accounting issues that have arisen within the context of the Standards and to give authoritative guidance (IFRIC Interpretations) on those issues. The Committee also provides other application support. For example, when the Committee decides it is not necessary to address an application question through standard-setting, it publishes an agenda decision. To the extent possible, these agenda decisions provide useful information—typically explaining how an entity applies the principles and requirements in the Standards to the specific circumstances in the question. Agenda decisions can also highlight relevant parts of a Basis for Conclusions or an Illustrative Example, as well as pointing to disclosures that might provide useful information to users of financial statements.

Summary

In this document, we have cast the adoption of the Standards in three steps: the policy decision, the plan and the resources.

This document is not a comprehensive discussion because, as stated earlier, each jurisdiction's adoption poses its own challenges.

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Frequently asked questions

If a jurisdiction decides to prohibit early adoption, can it still assert that it has adopted IFRS?

Yes, it can. The assertion about compliance with IFRS is made by an individual company in an individual set of financial statements. If a jurisdiction provides a framework that allows the company to make that assertion, then the jurisdiction can be said to have adopted IFRS. The company in Jurisdiction X might be prohibited from early adoption. The company's financial statements are not different from a company in Jurisdiction Y that could have adopted early but chose not to do so.