



IFRS: The Road to Conversion

Implications to KPMG and its Clients of Conversion to IFRS

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KPMG LLP

Today's Presenters

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Qualification on Information Provided

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your adviser.

Many of the opinions expressed during this presentation are those of the presenter and should not be considered the opinions of KPMG LLP or its Leadership.

Today's Agenda

Background

Challenges and Opportunities

The Impact from Conversion

Lessons from EU Adoption

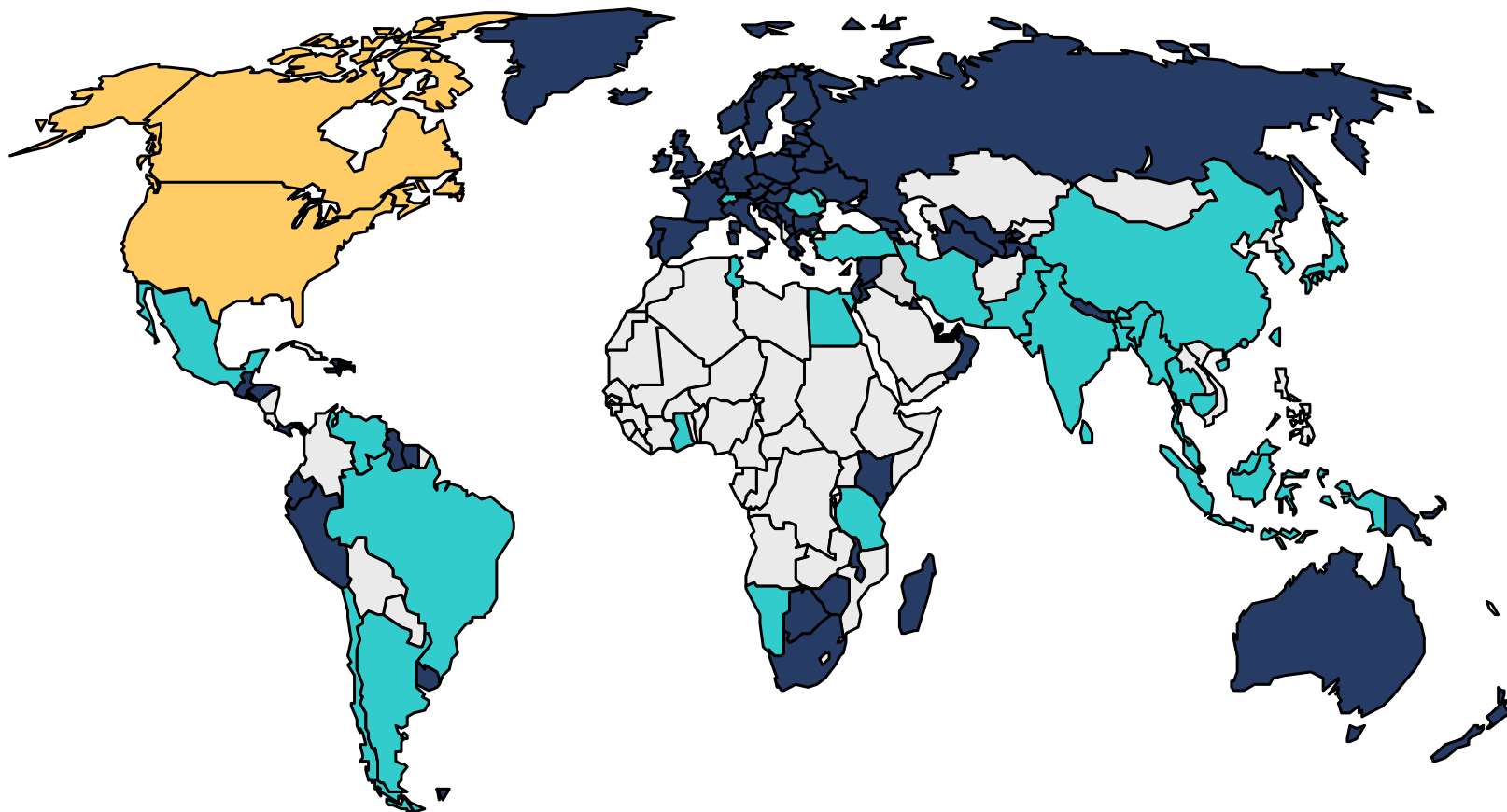
Training Challenges

KPMG Risk Management

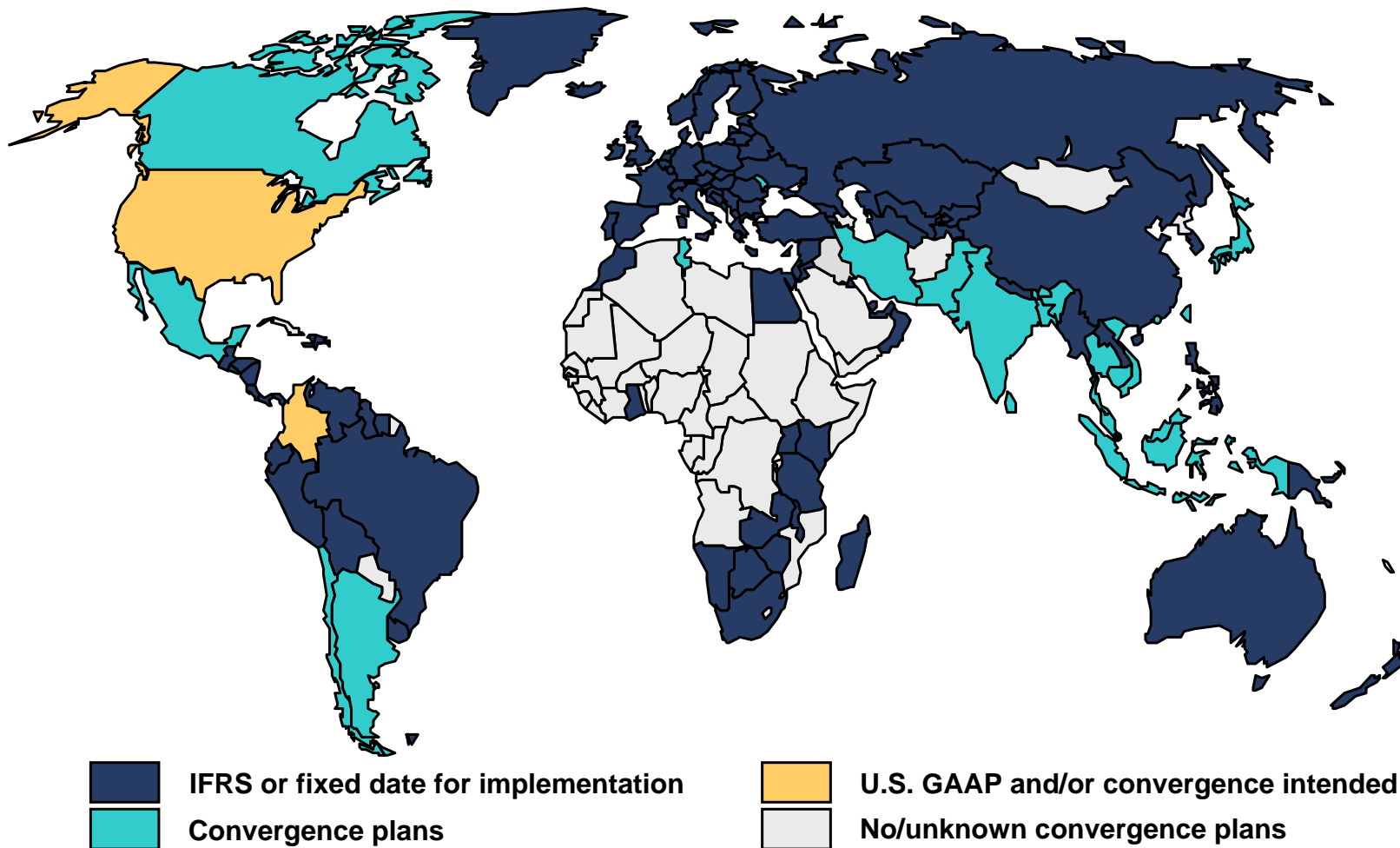
Who Uses IFRS?

- **Over 130 countries currently require the use of or have a policy of convergence with IFRS**
- **Increased globalization of capital and trade markets have led to increased pressures to harmonize**
- **Companies with an international footprint are finding IFRS to be preferable or necessary in many instances**
- **Most U.S. public companies are beginning to think about IFRS, and the impact it will have on their organizations in the coming years**

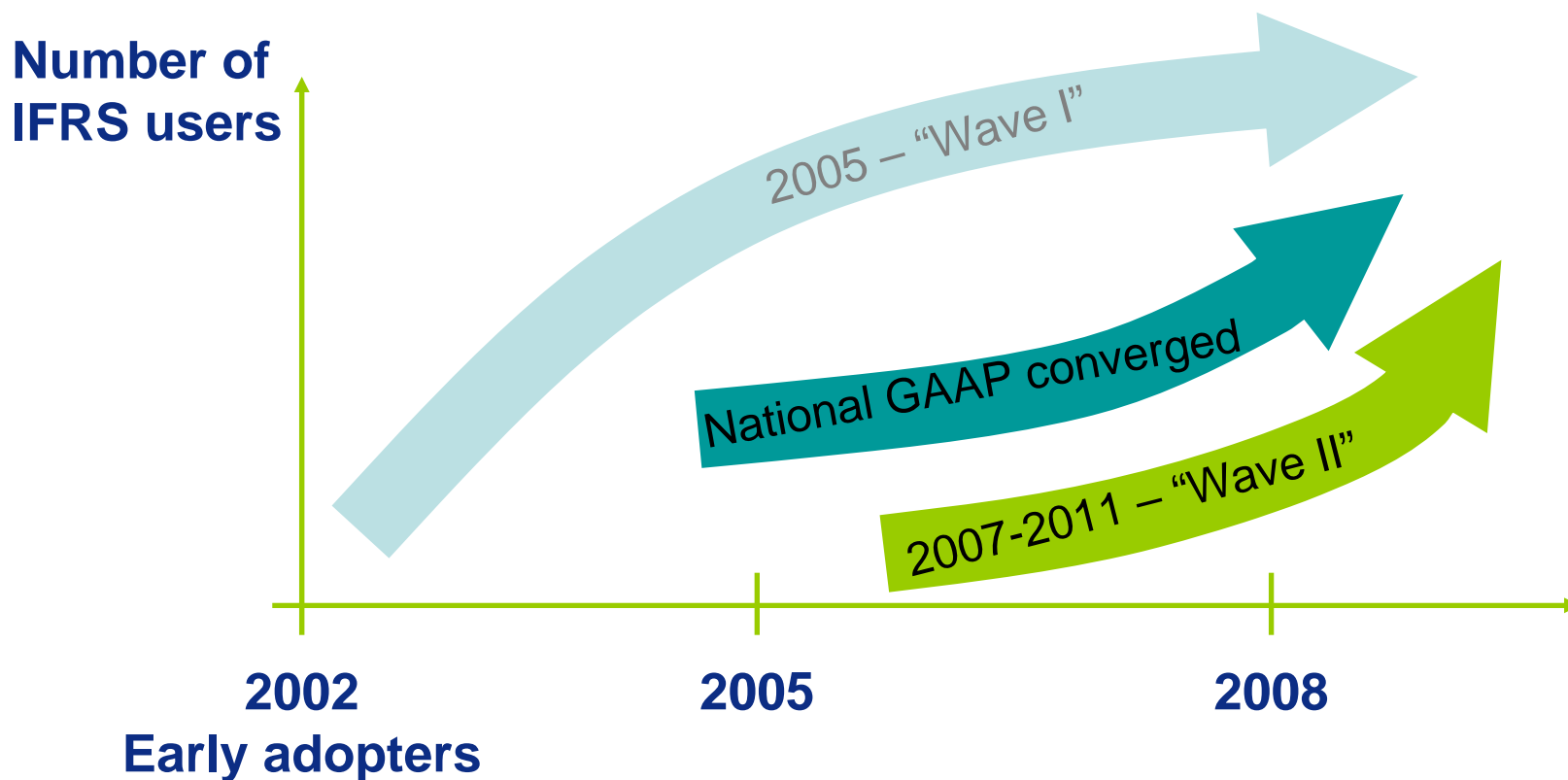
IFRS Implementation Around the World (2004)



IFRS Implementation Around the World (2008)



Converging on a bilingual world



Today, over 100 countries either require or allow the use of IFRS

“Wave II” is coming

- **Korea** **2011: IFRS mandatory for listed businesses – 2009: IFRS permitted**
- **Japan** **Goal of full convergence by 2011**
- **China** **Align Chinese GAAP with IFRS by 2011**
- **Israel** **Required for public companies from 2008**
- **India** **Convergence with IFRS for public companies for 2011**
- **Brazil** **Banks to be required to use IFRS starting from 2010**
- **Canada** **Timeframe set – 2011: Reporting under IFRS for publicly accountable entities**

2006 Summary IFRS to U.S. GAAP Reconciliation (1)

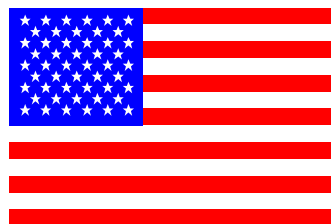
	Higher		Lower	
	Percentage of Filers	Median Difference	Percentage of Filers	Median Difference
Earnings	66%	12.9%	33%	9.1%
Equity	50%	6.6%	50%	12.7%

(1) The Analyst's Accounting Observer, Volume 16, No. 11 September 24, 2007







U.S. GAAP – IFRS Convergence

- The FASB and IASB have the objective of convergence of U.S. GAAP and IFRS
- Formal arrangement
- Major projects to be completed:

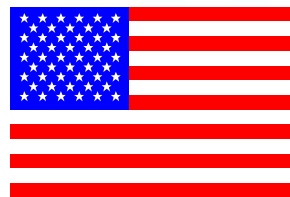
❖ Consolidations	❖ Derecognition
❖ Leases	❖ Financial Statement Presentation



Factors Driving Early Adoption

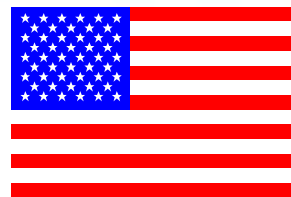
	Net Worth Date of Conversion	Future Earnings Impact
Asset Revaluation		
Onerous Contracts		
Unrecognized Pension Losses		

Be Careful What you Wish for!



	US GAAP	IFRS
LIFO	Permitted	Prohibited
Asset Impairment		
Other Than Temporary Impairment		
Enhancement of Pension Benefits		

Be Careful What you Wish for!



	US GAAP	IFRS
LIFO	Permitted	Prohibited
Asset Impairment	Less Frequent and Larger	More Frequent and Smaller
Other Than Temporary Impairment		
Enhancement of Pension Benefits		

Impairment of Long-lived Assets: Example 1

XYZ is assessing Unit A for impairment

Carrying value:	\$45m
Future undiscounted CFs	\$50m
Discounted CFs	\$40m
Fair value*	\$37m

What answers do you get
Under FAS 144?

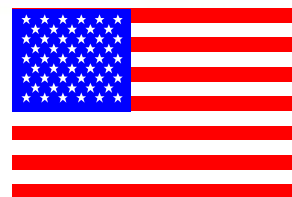
What about IAS 36?

*Costs to sell assumed to be
inconsequential

**US GAAP—future cash flows
are > CV
Therefore
NO impairment**

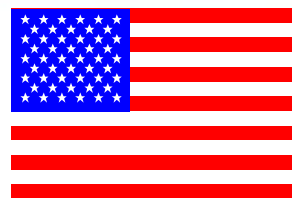
**IFRS—Recoverable amount is < CV
Therefore write-down to
the higher of value in use or fair value*
= \$5m impairment**

Be Careful What you Wish for!



	US GAAP	IFRS
LIFO	Permitted	Prohibited
Asset Impairment	Less Frequent and Larger	More Frequent and Smaller
Other Than Temporary Impairment	Amount AND Duration	Amount OR Duration
Enhancement of Pension Benefits		

Be Careful What you Wish for!



	US GAAP	IFRS
LIFO	Permitted	Prohibited
Asset Impairment	Less Frequent and Larger	More Frequent and Smaller
Other Than Temporary Impairment	Amount AND Duration	Amount OR Duration
Enhancement of Pension Benefits	Recognize over Service Lives	Recognize over Vesting Period

Prior Service Costs Example

- XYZ's defined benefit pension plan provided for retirees to receive 50% of their final year's pay from retirement date until their death
- As a result of negotiations with the unions, XYZ increased the benefit to 70% of their final year's pay beginning January 1, 20X7, creating a prior service cost of \$25 million allocated to the following groups (*average remaining service period is 20 years*):

<u>Group</u>	<u>Amount</u>
Retirees	\$6 million
Fully-vested employees	\$7 million
Unvested employees (vesting date: 12/31/X7)	\$5 million
Unvested employees (vesting date: 12/31/X8)	\$4 million
Unvested employees (vesting date: 12/31/X9)	\$3 million

What is the amount of expense to be recognized in 20X7 related to these prior service costs under U.S. GAAP and IFRS?

Prior Service Costs Example (continued)

U.S. GAAP

Since we do not have information for each individual employee, the prior service cost of \$25 million would be spread over the average remaining service period of 20 years resulting in additional expense of **\$1.25 million per year (\$25 million / 20 years)**

IFRS

XYZ would recognize \$21 million of the past service cost in 20X7, as follows:

	<u>Amount</u>
Retirees (fully vested)	\$ 6 million
Fully-vested employees	7 million
Unvested employees (fully vested at 12/31/X7)	5 million
Unvested employees (fully vested at 12/31/X8; \$4m/2yrs)	2 million
Unvested employees (fully vested at 12/31/X9; \$3m/3yrs)	<u>1 million</u>
TOTAL	\$21 million

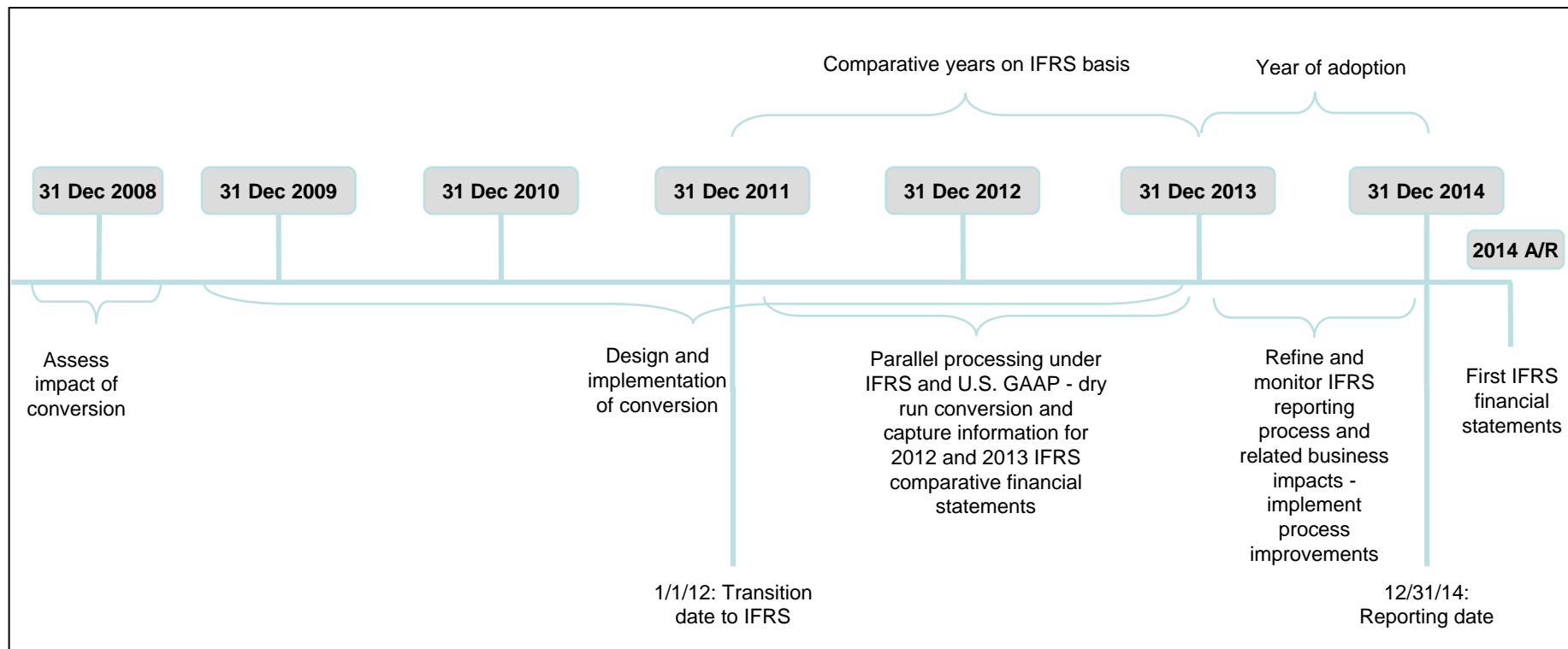
How Does IFRS Differ From U.S. GAAP?

- IFRS is a less extensive body of literature than is U.S. GAAP
 - ❖ In many instances, IFRS contains similar concepts but does not contain the same amount of detailed implementation guidance as U.S. GAAP
- Because of less-detailed guidance, there are more circumstances where application of IFRS will require exercise of judgment
 - ❖ Judgment will need to be supported by contemporaneous analysis
 - ❖ Clear, transparent disclosures of critical accounting policies and estimates
- **Two Critical Concerns**
 - ❖ Competitors Selection of Policies
 - ❖ Litigation Exposure

Key Take-aways: IFRS is not just an Accounting Exercise



IFRS Transition Milestones and Timeline – An Example 2014 Adopter



A/R – Annual Report

Potential Challenges When Adopting IFRS

- **Training**
- **IT system changes**
- **Changes to policies, procedures and controls**
- **Contractual and legal obligations**
- **Different type of professional judgment**
- **Communications with users**
- **Compensation plans and performance measurement**
- **Accounting policy selection issues**
- **Divergent management, income tax and inter-group reporting bases**
- **Corporate governance issues**
- **Risks of short-term financial reporting quality shortfalls**
- **Increased risk of misstatement, error, omission and fraud**
- **A learning curve**

Accounting and Reporting

- **Identify Differences**
 - Financial Reporting
 - Disclosures
- **Develop New Accounting Policies**
- **Assess Impact on Local Reporting**
- **Small Differences have Big Impacts**



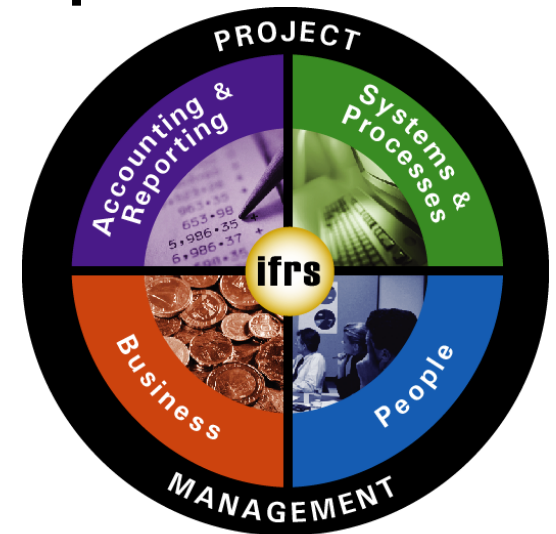
Systems and Processes

- Engage the IT team
- Modify data collection processes
- Embed IFRS in local ledgers
- Minimize manual workarounds
- Parallel System Runs



Business

- Communication plans to minimize surprises
- Internal measurement matrices
- Management compensation metrics
- General business issues
- Third-party contracts
- Budget for conversion



People

- Training
- Recruiting Experienced Resources
- Project Team Members
 - Cross Functional
 - All Major Geographies



What Have We Learned from the Adopters in EU and Australia?

■ Five Key Lessons

- **Underestimated the scale and complexity**
- **Senior management buy-in and board sponsorship is crucial**
- **Project teams were unprepared to deal with the technical issues**
- **Too many top-side “patchwork” solutions**
- **Underestimated time stakeholder and management teams took to get comfortable with the “new” numbers**

Training Considerations and Challenges

- **Institutional Knowledge is Based in US GAAP**
- **Audit vs. Advisory vs. Tax**
- **Conversion Project Training**
- **Application vs. Classroom Knowledge**
- **Timing**

KPMG's Current Approach to Training

- **Web-based topical sessions**
- **Baseline**
- **Advanced**
- **Conversion**
- **Client**

Approach to Risk Management

- **Ranking complexity of IFRS engagements**
- **IFRS Reviewing Partners**
- **Use of EU and Australian Professionals**

Where You Can Get More Information

- **The KPMG IFRS Institute is an open forum where board and audit committee members, executives, management, stakeholders and government representatives can share knowledge, gain insight and access thought leadership about the evolving global financial reporting environment. The website includes:**
 - Newsfeeds and Events
 - KPMG Briefing Sheets / Defining Issues
 - Regular webcasts and videocasts
 - Conferences and share forums
- **www.kpmgifrsinstitute.com**