

Why CFOs need to know about IFRS

International Financial Reporting Standards (IFRS) are the accounting rules all public companies in the European Union must follow, with another 100 countries either implementing or considering them. So why should this concern a US company? There are at least seven good reasons.

1. Convergence may eventually change US rules.

The Financial Accounting Standards Board (FASB) in the US and its international counterpart, the IASB, have been trying to minimize the differences between US GAAP and IFRS for some time. In a number of cases this has meant changing US GAAP to the IFRS position. One could interpret this as meaning that, in some respects, the US has lost sovereignty over US GAAP. The bottom line for a US company is that developments at the IASB are relevant and may portend future changes to US GAAP.

For example, IFRS was the first standard to require the expensing of stock options at fair value, and the FASB cited convergence with IFRS as one of the reasons for adopting this position, despite the concerns of some US stakeholders. Although the FASB had its usual comment period prior to making this rule final, in this case, US companies might have been better served by raising their issues in London, as well as with the FASB.

In another case, a recent IFRS exposure draft would require companies to record **all** contingent liabilities at fair value, no matter how unlikely they are to occur. If the proposed IFRS standard is adopted, the FASB is likely to consider making this change as well.

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- US companies whose debt or equity securities are traded on a European exchange may be required to publish certain IFRS information according to a recent directive from the Committee of European Securities Regulators (CESR). Since there currently is some lack of clarity regarding how much data companies will need to supply, management should discuss the potential impact of these new requirements with their advisors.

3. How important is it for your company to attract non-US investors?

As investors, analysts and other users of financial information embrace IFRS in Europe and elsewhere, a US company should consider whether releasing IFRS information will become a factor in attracting investors outside the US.

- ### 4. Where are your competitors?
- In global industries, key competitors may be based outside the US and use IFRS to report financial information, creating situations where a US company and its competitors report comparable transactions differently. Understanding these differences is vital to putting the financial performance of a competitor in perspective. A company that truly understands a competitor's performance can assess its ability to make strategic investments, or its potential exposure to regulatory actions. Such analyses may also reveal a competitive advantage.

For example, suppose several companies are competing on an acquisition or alliance. If one suitor uses US GAAP and the other IFRS, they could arrive at two significantly different estimates of how the transaction will affect earnings and balance sheet presentation. At the margin, the accounting standards used can also influence deal pricing and which structures various parties to the transaction are willing to accept.

- ### 5. IFRS will affect private companies and other accounting standards.
- Currently, IFRS applies only to public companies based in the EU. But in those countries, private companies contemplating an IPO or sale to a public company will find it advantageous to present financial information in IFRS. If a US-based company is considering selling or otherwise disposing of operations overseas, IFRS information may be needed.

Not only does it take time and resources to prepare this information, but key financial metrics on an IFRS basis could yield some surprises due to the differences relative to US GAAP.

6. Do you have the right resources in place? IFRS is converging with local accounting standards in the EU and elsewhere. As IFRS is often more complex than existing country standards, multinationals based outside the EU may have to add resources, since the necessary skills may not reside in the finance function of the many legal entities a typical multinational has around the world.

7. Will IFRS replace GAAP for tax purposes?

Lawmakers in any number of jurisdictions are contemplating extent to which IFRS should replace local GAAP as the basis for determining taxable income.

Given these developments, it is imperative that US companies understand IFRS so they can seize the opportunities and address the issues arising from acceptance of these standards in more and more countries worldwide. We will keep you abreast of developments as they occur. Stay tuned.

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