

**INTERNATIONAL PRACTICES TASK FORCE**  
**Center for Audit Quality Washington Office**  
**November 25, 2008**  
**HIGHLIGHTS**

The Center for Audit Quality (CAQ) SEC Regulations Committee's International Practices Task Force (the "Task Force") meets periodically with the Staff of the SEC to discuss emerging technical accounting and reporting issues relating to SEC rules and regulations. The purpose of the following highlights is to summarize the issues discussed at the meetings. These highlights have not been considered and acted on by senior technical committees of the AICPA, or by the Financial Accounting Standards Board, and do not represent an official position of either organization. In addition, these highlights are not authoritative positions or interpretations issued by the SEC or its Staff. The highlights were not transcribed by the SEC and have not been considered or acted upon by the SEC or its Staff. Accordingly, these highlights do not constitute an official statement of the views of the Commission or of the Staff of the Commission.

**I. Attendance**

Task Force Members

Paul Curth (Ernst & Young)  
Jon Fehleison (KPMG)  
Steven Krohn (KPMG)  
Michael Liesmann (PwC)  
Debra MacLaughlin (BDO)  
Joel Osnoss (Deloitte & Touche)  
Carol Riehl Banford (Grant Thornton)  
David Schmid (PricewaterhouseCoopers)  
Sondra Stokes (Deloitte & Touche)

Observers

Greg Burton (SEC Staff Observer)  
Jill Davis (SEC Staff Observer)  
Paul Dudek (SEC Staff Observer)  
Chris Holmes (SEC Regulations Committee Observer)  
Liza McAndrew Moberg (SEC Staff Observer)  
Craig Olinger (SEC Staff Observer)  
Annette Schumacher Barr (Center for Audit Quality Staff Observer)  
John Wolfson (SEC Regulations Committee Observer)

**II. Current Practice Issues Addressed in Discussion Documents\***

- A. First Time Adoption of IFRS by a FPI that Previously Used US GAAP for its primary financial statements in its 20-F**
- B. Applicability of Industry Guide 3 Disclosures for "Domestic" and "Foreign" Operations to IFRS (IASB) reporting FPIs**
- C. PCAOB audit opinion for significant obligors/swap counterparties of Reg AB filers**
- D. Follow-up on MJDS and Consents**
- E. Implementation of transition for change in accountant disclosures under the SEC's Foreign Issuer Reporting Enhancements ("FIRE") rules**
- F. Summary of Hyperinflationary Economies**

**III. Discussion of Document B from the June, 2008 Meeting *Venezuela Exchange Controls*\***

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\* Discussion documents are current only as of the date of the Task Force meeting. Users of these Highlights should consider developments subsequent to November 25, 2008 when applying the guidance presented herein.

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**Discussion Document A**

**Topic: First Time Adoption of IFRS by a FPI that Previously Used US GAAP for its primary financial statements in its 20-F**

**Background:**

Questions have arisen as to the application of the instruction 3 to Item 8 of Form 20-F. This instruction was added to Form 20-F as part of the Commission adopting an amendment to Form 20-F to allow an eligible FPI for its first year of reporting under IFRS to file two years rather than three years of statements of income, shareholders' equity and cash flows prepared in accordance with IFRS. Specifically, the issue relates to Instruction #3, which states:

3. If the primary financial statements included in the document represent the first filing by the issuer with the SEC of consolidated financial statements prepared in accordance with IFRS, the notes to the financial statements prepared in accordance with IFRS shall disclose the following:
  - a. The reconciliation from Previous GAAP to IFRS required by IFRS 1 shall be presented in a form and level of information sufficient to explain all material adjustments to the balance sheet and income statement and, if presented under Previous GAAP, to the cash flow statement; and
  - b. To the extent the primary financial statements reflect the use of exceptions permitted or required by IFRS 1, the issuer shall identify each exception used, including:
    - i. An indication of the items or class of items to which the exception was applied; and
    - ii. A description of what accounting principle was used and how it was applied.

Under IFRS 1, *First-time Adoption of IFRS*, a company that is presenting financial statements in accordance with IFRS for the first time is a "first-time adopter" and it should apply IFRS 1 in preparing its financial statements. IFRS 1 requires full retrospective application of IFRS in a company's first IFRS financials. This means that companies must retrospectively apply the current versions of IFRS for all periods presented (opening IFRS balance sheet, comparative period(s) and current period), except for those areas with specified limited relief as described in IFRS 1. The accounting policies that a company uses in its opening IFRS balance sheet may differ from those that it used for the same date under its Previous GAAP. As a result, adjustments will arise for certain events and transactions that took place before the date of transition to IFRS. Therefore,

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IFRS 1 provides that an entity shall recognize those adjustments directly in retained earnings (or, if appropriate, another category of equity) at the date of transition to IFRS, with limited exceptions.

As described above, IFRS 1, as a general principle, requires a first-time adopter to measure all assets and liabilities recognized in its opening IFRS balance sheet on the basis required by the relevant IFRS effective at the reporting date. However, in some cases, the process of reconstructing initial fully IFRS-compliant financial statements might be costly or burdensome, or even impracticable. To ease the burden, the IASB, considering these cost-benefit constraints, developed certain voluntary exemptions to the general principle. Companies are free to choose whether or not to avail themselves of each of these exemptions from applying other IFRS retrospectively. While IFRS 1 allows for voluntary exemptions from restatement, it also specifically prohibits restatement for certain transactions upon the initial adoption of IFRS, as the respective application in those areas would require judgments by management about past conditions after the outcome of the particular transactions (referred to as mandatory exceptions).

In addition, IFRS 1 requires certain disclosures to be made in a company's "first IFRS financial statements." These disclosures include, among other things, information about differences from a company's "previous GAAP" and IFRS. IFRS 1 requires the following:

**RECONCILIATIONS**

39. To comply with paragraph 38, an entity's first IFRS financial statements shall include:
- (a) reconciliations of its equity reported under previous GAAP to its equity under IFRSs for both of the following dates:
    - (i) the date of transition to IFRSs; and
    - (ii) the end of the latest period presented in the entity's most recent annual financial statements under previous GAAP;
  - (b) a reconciliation to its total comprehensive income under IFRSs for the latest period in the entity's most recent annual financial statements. The starting point for that reconciliation shall be total comprehensive income under previous GAAP for the same period or, if an entity did not report such a total, profit or loss under previous GAAP.
  - (c) if the entity recognised or reversed any impairment losses for the first time in preparing its opening IFRS balance sheet, the disclosures that IAS 36, Impairment of Assets, would have required if the entity had recognised those impairment losses or reversals in the period beginning with the date of transition to IFRSs.
40. The reconciliations required by paragraph 39(a) and (b) shall give sufficient detail to enable users to understand the material adjustments to the balance sheet and income

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statement. If an entity presented a cash flow statement under its previous GAAP, it shall also explain the material adjustments to the cash flow statement.

41. If an entity becomes aware of errors made under previous GAAP, the reconciliations required by paragraph 39(a) and (b) shall distinguish the correction of those errors from changes in accounting policies.
42. IAS 8 does not deal with changes in accounting policies that occur when an entity first adopts IFRSs. Therefore, IAS 8's requirements for disclosures about changes in accounting policies do not apply in an entity's first IFRS financial statements. [Paragraph 42 amended by paragraph A23 of IAS 8.]
43. If an entity did not present financial statements for previous periods, its first IFRS financial statements shall disclose that fact.

Many FPIs prepare their financial statements in accordance with U.S. GAAP for SEC reporting purposes. However, in light of the recent elimination of the U.S. GAAP reconciliation and as regulators in other countries around the world either permit or require the use of IFRS in their local country filings, companies are now contemplating the use of IFRS for SEC reporting purposes. As a result, certain questions have arisen in connection with the timing of adoption of IFRS for purposes of filings with the SEC vis-à-vis the timing of adoption of IFRS in the FPI's home country.

**Discussion:**

The questions are discussed in the context of the following scenarios.

**Scenario A – The FPI adopts IFRS in the current period for both local and SEC reporting purposes.**

Company X is publicly listed in its home country and is a foreign private issuer that files on Form 20-F. In its home-country consolidated annual report and for SEC reporting purposes, Company X will adopt IFRS as issued by IASB (“IFRS”) for the first time for financial year 2008 with a transition date of January 1, 2007. Therefore, financial year 2008 will be the first time that the primary financial statements prepared in accordance with IFRS will be filed with the SEC. The table below summarizes the GAAP that Company X has applied in the home country consolidated annual report and in filings with the SEC.

	2004	2005	2006	2007	2008
<b>GAAP Used in Local Report</b>	Local GAAP	Local GAAP	Local GAAP	Local GAAP - IFRS	IFRS
<b>Primary GAAP</b>	US GAAP	US GAAP	US GAAP	US GAAP	IFRS

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Filed with the SEC					
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In Scenario A, Company X has made the determination that Local GAAP is the Previous GAAP for purposes of developing an initial fully IFRS-compliant set of financial statements. The instructions to Item 8 of Form 20-F require a reconciliation from Previous GAAP to IFRS, as required by IFRS 1, upon first time adoption of IFRS, and the reconciliation would need to be disclosed in the financial year 2008 financial statements included in the Form 20-F.

Questions:

**1) Does the Staff believe that the inclusion of the IFRS 1 reconciliation (from Local GAAP to IFRS) in the audited IFRS financial statements in the current SEC filing satisfies the requirements of Form 20-F?**

View 1: Yes. The inclusion of the IFRS 1 reconciliation in the audited financial statements satisfies the instructions to Item 8 of Form 20-F, which require that such a reconciliation be included in the notes to the first IFRS financial statements filed with the SEC.

View 2: No. While the inclusion of the IFRS 1 reconciliation in the audited financial statements may satisfy the instructions to Item 8 of Form 20-F, supplemental disclosure about the differences between US GAAP and IFRS would be necessary to provide transparent information in connection with the FPI's adoption of IFRS to investors in the US capital markets, who previously would have had limited or no access to Local GAAP information. The disclosure should provide sufficient detail to enable users to understand the material reconciling items between the U.S. GAAP and IFRS balance sheet, income statement and, if applicable, cash flow statement.

When the Commission considered the new Instruction 3 to Item 8 of Form 20-F it did not propose, and did not adopt, specific form or content requirements for the reconciliation from Previous GAAP. Rather, the Commission noted that a reconciliation following example 11 under Implementation Guidance 63 of IFRS 1 or a reconciliation based on the form and content provisions of Item 17 would meet the requirement.

Given the Commission's elimination of the requirement to reconcile to U.S. GAAP for foreign private issuers preparing their financial statements in accordance with IFRS, there would not be any form of reconciliation from IFRS to U.S. GAAP in Company X's 2008 financial statements in the filing with the SEC.

The bridging reconciliations between IFRS and US GAAP should be presented for the same periods and dates for which IFRS 1 reconciliations are required. Although not specified by IFRS 1, the bridging disclosure is consistent with the IASB's stated objective in IFRS 1, BC 91: "... The Board concluded that such disclosures are essential ... because they help users understand the effect and implications of the transition to IFRSs and how they need to change their analytical models to make the best use of information presented using IFRSs

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...”, This disclosure is intended to bridge the users’ understanding of the Company’s financial position and results from US GAAP to IFRS. Because each foreign private issuer’s situation will be different, the proponents of this View do not believe a prescriptive approach to the information to be included in the reconciliation would be practicable or desirable if this view prevails.

As a variation to Scenario A, proponents of View 2 would provide the supplemental disclosures for any SEC registrant who has provided full US GAAP financial statements on Form 20-F in the past, has not identified US GAAP as its Previous GAAP for purposes of first time adoption of IFRS, and will continue to use Local GAAP in its local filings. For example, the supplemental disclosures would be provided if Company X:

- a) is adopting IFRS for purposes of its SEC filing only, and
- b) has determined that Previous GAAP is Local GAAP (based in part on Company X’s expectation that its home-country regulator will eventually require or permit adoption of IFRS, and require Company X to include some form of an IFRS 1 reconciliation in its first home-country filing containing IFRS financial statements), and therefore, includes a reconciliation from Local GAAP to IFRS (rather than from US GAAP to IFRS) in its audited IFRS financial statements in the current SEC filing.

The table below summarizes this variation of scenario A.

	2004	2005	2006	2007	2008
<b>GAAP Used in Local Report</b>	Local GAAP	Local GAAP	Local GAAP	Local GAAP	Local GAAP
<b>Primary GAAP Filed with the SEC</b>	US GAAP	US GAAP	US GAAP	US GAAP	IFRS

**SEC Staff Response:**

The Staff believes that additional disclosure is necessary to provide US investors with information to help bridge from U.S. GAAP that had previously been reported in the Form 20-F to IFRS. At a minimum, the Staff would expect such disclosure to contain sufficient information to enable users to understand the material reconciling items between the US GAAP and IFRS financial statements. In most cases, this could consist of either of the following two alternative disclosures:

Alternative 1: An analysis of the differences between U.S. GAAP and IFRS in a format consistent with the form and content provisions of Item 17 for the same periods and dates for

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which IFRS 1 reconciliations are required. This analysis would disclose differences between U.S. GAAP and IFRS for equity as of the beginning and end of the most recent comparative period to the year of adoption and of profit or loss for the most recent comparative year then ended. A description of differences between U.S. GAAP and IFRS as they relate to the statement of cash flows would not be necessary, since under its accommodation to foreign private issuers, the Commission accepts without reconciliation to U.S. GAAP a cash flow statement prepared in accordance with IAS 7, "Cash Flow Statements," as amended<sup>†</sup>.

or,

Alternative 2: "Two-step reconciliations" of equity as of the beginning and end of the most recent comparative period to the year of adoption and of profit or loss for the most recent comparative year then ended. The "two-step reconciliations" would present: (Step 1) a quantitative analysis of the differences between U.S. GAAP and Previous GAAP, consistent with an Item 17 format for the same periods and dates for which IFRS 1 reconciliations are required; and (Step 2) the IFRS 1 reconciliation from Previous GAAP to IFRS. In addition to this reconciliation, an explanation of the material differences between the cash flow statement under U.S. GAAP and the cash flow statement under previous GAAP for the most recent comparative period to the year of adoption should also be provided.

Although generally the Staff would expect to see the analysis in either of the formats it has described above, the Staff would be willing to consider requests to provide other presentations, based on unique or unusual circumstances.

In the case of the variation on scenario A presented above, the Staff believes that either of the two alternative disclosures described above may be provided.

**2) A second question arises as to whether the additional disclosure should be included in the audited financial statements or in Item 5 of Form 20-F?**

Considering the Staff's response to Question 1 above, a follow-up question arises as to whether the additional disclosure should be in Item 5 of Form 20-F, or included in the audited financial statements.

View 1: The additional disclosure that provides US investors with information to help bridge from the U.S. GAAP information that had previously been reported in the Form 20-F to IFRS should be included in Item 5 of Form 20-F. View 1 proponents note that the additional disclosure, as described above, is not required by IFRS 1. Furthermore, authoritative literature does not address accounting for a change in accounting basis. Rather, US GAAP and IFRS provide guidance for reporting accounting changes within the same basis. However, the above scenario is considered to be a change in accounting basis rather than an accounting change.

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<sup>†</sup> Item 17(c)(2)(iii) of Form 20-F

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In the recently published proposed Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers<sup>‡</sup>, the Commission proposes for comment, inter alia, the presentation of a supplemental reconciliation from IFRS to U.S. GAAP by those domestic registrants permitted to adopt IFRS as early as 2009, and it is proposed that such reconciliation be unaudited. View 1 proponents also note that often FPIs that prepare financial statements in accordance with IFRS for their local annual report to shareholders simply include the financial statements from the local annual report for purposes of Form 20-F filing, and therefore, it would seem more practical and efficient to include supplemental US GAAP information in Item 5 as opposed to adding to the financial statements.

View 2: The additional disclosure should be included in the audited financial statements. While not explicitly required by IFRS or US GAAP, proponents of View 2 believe that the additional disclosure would be an integral part of the audited financial information provided to US investors. Given the context of a wholesale change in the accounting principles used to prepare the financial statements, this additional disclosure should be included in the audited financial statements.

**SEC Staff Response:**

The Staff agrees with View 2. If the registrant determines that it is impractical to include the additional disclosure related to US GAAP information in the audited financial statements, the Staff would not object to the registrant including the additional disclosure related to US GAAP information in an audited supplemental financial statement schedule.

**Scenario B – The FPI adopted IFRS in a period that precedes the earliest period for which audited financial statements are required to be included in the current SEC filing.**

Company Y is publicly listed in its home country and is a foreign private issuer that files on Form 20-F. In its local home country consolidated annual report, Company Y adopted IFRS as issued by the IASB for the first-time for financial year 2005 with a transition date of January 1, 2004. For purposes of the transition to IFRS, Company Y has made the determination that Previous GAAP is Local GAAP. For SEC reporting purposes, Company Y decided to present its financial statements in accordance with US GAAP from January 1, 2004. For financial year 2008, following the elimination of the US GAAP reconciliation, Company Y has decided to use its IFRS financial statements in its Form 20-F filed with the SEC. Therefore, financial year 2008 will be the first time that the primary financial statements prepared in accordance with IFRS will be filed with the SEC.

The table below summarizes the GAAP that Company Y has applied in the primary financial statements in the local home country consolidated annual report and filings with the SEC.

	2003	2004	2005	2006	2007	2008
<b>GAAP Used in</b>	Local GAAP	Local GAAP -	IFRS	IFRS	IFRS	IFRS

<sup>‡</sup> See Release No. 33-8982, p. 70

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<b>Local Report</b>		IFRS				
<b>Primary GAAP Filed with the SEC</b>	Local GAAP With a reconciliation	US GAAP	US GAAP	US GAAP	US GAAP	IFRS

It should be noted that since the initial adoption of IFRS occurred in a year prior to those presented in Company Y's current filing, there is no requirement for the disclosures in IFRS 1 in the audited financial statements included in the current SEC filing.

Questions:

**1) A literal reading of the instructions to Item 8 of Form 20-F<sup>§</sup> would indicate that Company Y's first audited IFRS financial statements would be required to include the following information:**

- **a reconciliation of equity reported under Local GAAP to its equity under IFRS as of January 1, 2004;**
- **a reconciliation of equity reported under U.S. GAAP to its equity under IFRS as of December 31, 2007;**
- **a reconciliation of the profit or loss reported under U.S. GAAP to its profit or loss under IFRS for 2007; and**
- **an explanation of material adjustments to the cash flow statement under U.S. GAAP to the cash flow statement under IFRS for 2007.**

**Does the Staff believe that this literal reading is appropriate?**

View 1: No. The disclosure called for by the instructions to Item 8 of Form 20-F was intended to be consistent with the disclosures required by IFRS 1. The disclosure that would be provided based on such a literal reading of the instructions would neither comply with IFRS nor be meaningful to investors.

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<sup>§</sup> According to the instructions to Item 8 of Form 20-F, an entity's first IFRS financial statements are required to include (pursuant to IFRS 1), *inter alia*:

“(a) reconciliations of its equity reported under previous GAAP to its equity under IFRSs for both of the following dates:

- (i) **the date of transition to IFRSs** (emphasis added); and
- (ii) the end of the latest period presented in the entity's most recent annual financial statements under previous GAAP;

(b) a reconciliation of the profit or loss reported under previous GAAP for the latest period in the entity's most recent annual financial statements to its profit or loss under IFRSs for the same period”

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View 2: Yes.

**SEC Staff Response:**

**The Staff agrees with View 1.**

**2) Does the Staff believe that the IFRS 1 reconciliation disclosure from its year of adoption (2004) should be included in the current SEC filing?**

View 1: No.

View 2: Yes, the IFRS 1 reconciliation disclosure from its year of adoption (2004) should be included in the audited financial statements in the current SEC filing.

View 3: Yes, the IFRS 1 reconciliation disclosure from its year of adoption (2004) should be included as a supplemental unaudited disclosure.

**SEC Staff Response:**

**The Staff agrees with View 1.**

**3) Does the Staff believe that additional disclosure between US GAAP and IFRS (e.g., a reconciliation) would be necessary?**

View 1: No.

View 2: Yes.

**SEC Staff Response:**

The Staff agrees with View 2. The Staff notes, however, that the “two-step reconciliations” described in Alternative 2 under Scenario A above would not be practicable under Scenario B, due to the absence of Previous GAAP information for the most recent comparative year prior to the adoption year for purposes of the filing with the Commission, and, therefore, Alternative 1 may be the more practicable option. The additional disclosure would be provided for equity as of the end of the most recent comparative period in the Form 20-F and of profit or loss for the two most recent comparative years then ended. However, if the company presents a balance sheet as of the end of the third preceding year in accordance with IFRS, then the additional disclosure also would be provided for equity as of that date.

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**Discussion Document B**

**Topic: Applicability of Industry Guide 3 Disclosures for “Domestic” and “Foreign” Operations to IFRS (IASB) reporting FPIs**

**Background:**

A Foreign Private Issuer (FPI) which is a bank holding company is required to apply the disclosure requirements of SEC Industry Guide 3 (Guide 3) to the description of business portions of bank holding company registration statements for which financial statements are required. Generally, these disclosures are incorporated in the Management's Discussion and Analysis section of Form 20-F.

Industry Guide 3 requires disclosures for both “Domestic” and “Foreign” operations. The disclosure is triggered by General Instruction 7 of Guide 3 which states that:

"In various places throughout this Guide, disclosure is called for regarding certain "foreign" data. For purposes of the Guide, this information need not be presented unless the registrant is required to make separate disclosures concerning its foreign activities in its consolidated financial statements pursuant to the test set forth in Rule 9-05 of Regulation S-X"

In the SEC’s release (footnote 136, page 58), Acceptance from Foreign Private Issuers of Financial Statements Prepared In Accordance with International Financial Reporting Standards Without Reconciliation to GAAP, notes “Foreign private issuers that file financial statements prepared in accordance with IFRS as issued by the IASB will comply with IASB requirements for form and content within the financial statements, rather than with the specific presentation and disclosure provisions in Articles 4, 5, 6, 7, 9, and 10 of Regulation S-X.”

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**Issue # 1:**

If an FPI files financial statements prepared in accordance with IFRS as issued by the IASB (IFRS FPIs) with the SEC and are not required to comply with Article 9 of Regulation S-X, must an FPI, present such “Foreign” data required by Guide 3?

**View 1:** For IFRS FPIs that are bank holding companies, the form and content requirements of its financial statements are reflected in IFRS rather than in Regulation S-X. Therefore, IFRS FPIs are no longer subject to the foreign activities disclosures prescribed by Rule 9-05 of Regulation S-X. Consequently, Guide 3 foreign data disclosures would not be required as such Guide 3 disclosures are deemed contingent on a registrant having to provide such disclosures under Rule 9-05. Moreover, IFRS 7 requires certain disclosures about market risk and credit risk. Therefore, material foreign exposures would be provided in the financial statements.

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**View 2:** Although IFRS FPIs that are bank holding companies would not be required to follow Article 9 of Regulation S-X with respect its specific presentation and disclosure provisions within the financial statements, such registrants still need to comply with Guide 3. Guide 3 points to the test in Rule 9-05 of Regulation S-X merely for determining whether foreign data is material for disclosure. Therefore, even if IFRS FPIs are not required to comply with Article 9 disclosures, if foreign data is material from an Industry Guide 3 perspective (e.g. data exceeds the thresholds under Rule 9-05) the foreign data disclosures should be provided in addition to any IFRS 7 disclosures. In March 2008, the Task Force developed an implementation questions document that included Question 18 regarding Industry Guides as follows:

Q18. The SEC did not propose, nor did it adopt, any specific amendments with respect to information to be disclosed pursuant to Industry Guides. For example, Industry Guide disclosure is intended to provide a “track-record” of trend information such as loan quality information for banks providing disclosure under Industry Guide 3 or property casualty loss reserve development under Industry Guide 6. Are FPIs that prepare their financial statements in accordance with IFRS as issued by the IASB required to continue to provide the Industry Guide Information?

- A. Yes. FPIs should continue to provide the disclosures required by the Industry Guides. However, the disclosures should be based on information determined in accordance with IFRS as issued by the IASB.

Based on the above, the IFRS FPIs that are bank holding companies should continue to provide the disclosures required by Industry Guide 3.

**SEC Staff Response:**

**The Staff supports View 2.**

**Issue # 2:**

For IFRS FPIs, if an SEC disclosure requirement points to test or threshold included within an Article or Rule that is based on US GAAP and no longer applicable to IFRS FPIs (e.g. Articles 4, 5, 6, 7, 9, and 10 of Regulation S-X), is the disclosure no longer required for IFRS FPIs even if otherwise required when applying the test or threshold to IFRS amounts?

For example, although IFRS FPIs are still subject to Article 12 of Regulation S-X, the underlying test to determine whether disclosure is required for parent only information is provided under Rule 5-04 of Regulation S-X. Rule 5-04 itself is no longer applicable to IFRS FPIs.

Assuming that the threshold for disclosures under Rule 5-04 of regulation S-X are met using IFRS amounts, would the parent only information be required for an IFRS FPI?

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**View 1: No.** For IFRS FPIs, the form and content requirements of its financial statements are reflected in IFRS rather than in Article 4, 5, 6, 7, 9, or 10 of Regulation S-X. As such, since IFRS FPIs would not be subject to the disclosure requirements of Article 5--which the rules for filing financial statement schedules, the parent only schedule (Schedule I) would not be required.

**View 2: Yes.** As Article 12 still applies for IFRS FPIs, the fact that a test for determining whether disclosure is required under Article 12 is contained in Article 5 does not eliminate the disclosure requirement under Article 12. Therefore, if parent only information exceeds the thresholds described in Rule 5-04 using IFRS amounts, such information should be provided. In general while Regulation S-X would not modify the requirements of disclosures within the IFRS financial statements, the requirements for additional financial data, schedules or financial statements would still apply to FPIs. The Task Force notes in this regard that in the recently published proposed Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers<sup>\*\*</sup>, the Commission proposes that in the event IFRS is adopted, Article 12 would nevertheless continue to apply in its entirety.

**SEC Staff Response:**

**The Staff supports View 2.**

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<sup>\*\*</sup> See Release No. 33-8982, p. 88

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**Discussion Document C**

**Topic: PCAOB audit opinion for significant obligors/swap counterparties of Reg AB filers**

Regulation AB sections 1112 and 1115 set forth quantitative requirements for determining whether financial information for significant obligors or derivative counterparties, respectively, are required to be included or incorporated by reference in an asset-backed security issuers' Registration Statement or Annual Report.

Financial statements in compliance with the requirements of Regulation S-X, (except that they would not be required to comply with Rule 3-05 and Article 11 of Regulation S-X) should be provided by the significant obligor or derivative counterparty, respectively whether:

- pool assets relating to a significant obligor represent 20% or more of the asset pool under Section 1112, or
- the aggregate significance percentage related to any entity or group of affiliated entities providing derivative instruments is 20% or more under Section 1115.

Additionally, instructions allow that if the significant obligor is a foreign business, “the financial statement requirements may be complied with by providing financial statements meeting the requirements of Item 17 of Form 20-F for the periods specified by Item 8.A. of Form 20-F.”

**Which auditing standards should be referred to in the opinions related to the financial statements filed under a Regulation AB filing to comply with sections 1112 and 1115?**

**View 1:** The opinions of the swap counterparty and the significant obligor should refer to PCAOB standards regardless of whether entities are registrants or not. Compliance with the financial statement requirements of the swap counterparty and the significant obligor may be met by providing financial statements meeting the requirements of Item 17 of Form 20-F. As Item 17(a) requires financial statements for the same fiscal years and accountants' certificates that would be required to be furnished if the registration statement were on Form 10 or the annual report on Form 10-K and since such audit opinion should refer to PCAOB standards, the audit opinions should refer to PCAOB standards. Additionally, for entities that do not file a 20-F, as the financial statements are being incorporated into an SEC filing and by analogy to the Item 17(a) requirements, the audit of such financial statements should be conducted in accordance with PCAOB standards.

**View 2:** To the extent the swap counterparty or significant obligors are registrants, the opinion should refer to PCAOB standards. Nevertheless, if the swap counterparty or significant obligors are not registrants, SEC Rules generally do not require these financial statements to be audited by a registered public accounting firm or the audit to be conducted in accordance with PCAOB standards. Therefore, the opinion would not need to refer to PCAOB standards. This would be consistent to non-registrant financial statements that are filed under Rules 3-05, 3-09, 3-14, or 3-16 of Regulation S-X and for which the audit of the non-registrant is not relied upon for purposes of the registrants' audit. Consequently, the financial statements of non-registrant swap counterparties or significant obligors would not have to have the audit conducted in accordance with PCAOB

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standards but it would be required for the audit to be conducted in accordance with US generally accepted auditing standards.

**SEC Staff Response:**

**The Staff supports View 2.**

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**Discussion Document D**

**Topic: Follow-up on MJDS and Consents**  
**Background**

The subject of the inclusion of Canadian consents in MJDS filings was discussed at a March 22, 2005 meeting of the AICPA International Practices Task Force (see Appendix B ). The Task Force concluded that registrants should not be required to include the Canadian consent (i.e., the CICA 7110 consent as described below) in an MJDS filing with the SEC. However, SEC staff at the meeting noted that many registrants were including both consents and indicated “this appeared to be the appropriate practice”. SEC staff expressed a willingness to discuss the matter further with interested parties. The Canadian affiliates of a number of independent auditors of Canadian U.S. SEC registrants have raised this issue to the Task Force for further consideration under the continuing belief that the Canadian consent should be removed from MJDS filings in the U.S. This paper is intended to facilitate such further discussion.

In November 2003 Section 7110 of the CICA Handbook (“CICA 7110”) introduced a requirement for auditors to include in an offering document a specified form of consent (the “CICA 7110 consent”) in order to demonstrate that they have been involved with the document (see excerpt from CICA 7110 in Appendix A). The “inspiration” for including an auditor’s consent in an offering document came from the SEC requirement for an auditor’s consent to be included as an exhibit to a registration statement. With this SEC requirement in mind, CICA 7110 expressly provides for the consent included in a foreign offering document (e.g. a jurisdiction outside of Canada) to use the consent wording commonly used in the foreign jurisdiction. In the case of an SEC registration statement, the standard U.S. SEC form of auditor’s consent included as an exhibit to the registration statement serves the dual purpose of satisfying the SEC’s consent requirement and the Canadian auditor’s professional obligation under CICA 7110 to include his or her consent in the offering document.

**The issue**

Is it necessary to include the Canadian consent from the MJDS registration statement in a U.S. prospectus?

**View 1:**

No. The inclusion of both a Canadian and US consent for the use of a single audit report may be confusing to the users of a US prospectus. In addition, as described below in detail, the form, content and intended use of the Canadian consent is mandated by Canadian auditing standards and may not be appropriate for use outside of Canada.

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**Factors supporting exclusion of the CICA 7110 consent**

In general, the U.S. prospectus "...need not contain any disclosure applicable solely to Canadian offerees or purchasers that would not be material to offerees or purchasers in the United States". The MJDS forms proceed "without limitation" to provide a list of five specific examples of such disclosure. The CICA 7110 consent is not mentioned in these examples.

However, the MJDS forms were developed before the CICA 7110 consent came into existence and therefore could not have been considered when the above list of examples was formulated. In such circumstances we believe it is appropriate to evaluate new and unforeseen issues by analogy to the general characteristics of permitted exclusions and any related specific examples and have done so in outlining several of the following supporting factors.

**1. The CICA 7110 consent in the short form prospectus is intended solely for the Canadian offerees or purchasers under the short form prospectus**

As stated in CICA 7110.66 the reason for including the consent in the offering document is "...to demonstrate to readers that the auditor has been involved with the document". The CICA 7110 consent must identify the document in which the auditor's report appears. The CICA 7110 consent in the short form prospectus is intended for the Canadian offerees or purchasers who are entitled under Canadian securities legislation to receive the short form prospectus.

**2. The CICA 7110 consent is not included in a short form prospectus to satisfy a prospectus disclosure requirement**

The appearance of the CICA 7110 consent in a Canadian short form prospectus is the direct result of the auditor's compliance with the professional standards in CICA 7110. It is not provided pursuant to any prospectus disclosure requirement under Canadian securities legislation. Further, the CICA 7110 consent is prepared in accordance with the guidance in CICA 7110. Its content is not governed by any disclosure requirements under Canadian securities legislation.

**3. A Canadian auditor's consent is not material to offerees or purchasers in the United States**

The MJDS forms include the consent of an expert under the category of information not required to be delivered to the U.S. offerees or purchasers. The consent of an expert is required to be filed as an exhibit to the U.S. registration statement. It is apparent that an auditor's consent is not considered to be material to the U.S. offerees or purchasers who receive the U.S. prospectus. We do not see how the CICA 7110 consent could be regarded as being material to U.S. offerees or purchasers when a U.S. prospectus is not required to, and generally does not, include the consents of experts.

**4. The CICA 7110 consent included in the short form prospectus is integrally related to the certificates of the issuer and the underwriters**

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CICA 7110.67 permits the auditor to issue the consent only when the offering document has been approved by appropriate officials of the issuer. No auditor would consider issuing the consent until and unless management and the underwriters are ready to provide the prospectus certificates required under Canadian securities legislation. Conversely, management and the underwriters would not consider signing these certificates if the auditor were not ready to provide his or her consent. These certificates and the auditor's consent are integrally related. The CICA 7110 consent is almost always presented on a separate page of the short form prospectus immediately preceding the certificates of the issuer and the underwriters. We believe the expressly permitted removal of the certificates of the issuer and the underwriters, by analogy, supports the removal of the CICA 7110 consent in recognition that it is being replaced by the corresponding SEC form of consent.

**5. The CICA 7110 consent is not a report**

Experience has shown that the CICA 7110 consent may be open to misinterpretation, particularly in jurisdictions outside of Canada. For example, the CICA 7110 consent included in a U.K. prospectus has been regarded by the U.K. securities regulator as the report of an expert and Canadian issuers have been required to file the auditor's consent to the use of his or her CICA 7110 consent in the prospectus. We believe the source of the misunderstanding arises from the statements in the CICA 7110 consent that the auditor has read the prospectus and has complied with Canadian generally accepted standards for an auditor's involvement with offering documents. These are intended to be factual statements providing a context or point of reference for the nature and extent of the auditor's involvement.

***View 2:***

Yes. Proponents of View 2 note that many MJDS registrants are including the consent as part of the MJDS prospectus filed with the SEC. Because the offering document filed with the SEC under the MJDS is supposed to include the entire Canadian prospectus (subject to limited exceptions), this appears to be the appropriate practice.

**SEC Staff Response:**

The staff notes that the list of disclosure items enumerated in the MJDS forms which may be omitted for a U.S. prospectus is not an exclusive list. The issuer, as advised by its counsel, accountants and others involving in the offering, must evaluate and make the determination that omitted disclosure meets the criteria specified in the relevant MJDS form, i.e., that the disclosure is "applicable solely to Canadian offerees or purchasers that would not be material to offerees or purchasers in the United States." When the issuer makes this determination and, if requested by the SEC staff provides adequate support for this determination, the SEC staff would not object to the omission of the CICA 7110 consent.

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Appendix A:

**Excerpt from CICA Handbook Section 7110**

7110.68 A consent issued by the auditor should:

- (a) identify the document in which the auditor's report appears;
- (b) identify the auditor's report and any reservations therein;
- (c) identify the financial statements or other information on which the auditor is reporting;
- (d) express the auditor's consent to the use of the report in the document;
- (e) state that the auditor has read the document and has also complied with Canadian generally accepted standards for an auditor's involvement with offering documents; and
- (f) be dated concurrently with the document. [NOV. 2003 \*]

7110.69 The auditor's consent to the use of his or her audit report to be included in a prospectus or short form prospectus issued in Canada<sup>14</sup> might be worded as follows.

**AUDITOR'S CONSENT**

I have read the [short form] prospectus of X Limited (the Company) dated March 15, 20X5 relating to the issue and sale of [description of securities offered] of the Company. I have complied with Canadian generally accepted standards for an auditor's involvement with offering documents.

I consent to the [use / incorporation by reference] in the above-mentioned prospectus of my report to the [directors / shareholders] of the Company on the balance sheets of the Company as at December 31, 20X4 and 20X3, and the statements of earnings, retained earnings and cash flows for each of the years in the [three- / two-year] period ended December 31, 20X4. My report is dated February 15, 20X5 (except as to note ... which is as of March 15, 20X5).

City (signed) .....  
Date CHARTERED ACCOUNTANT

14 When an offering document is issued in another country, it would normally be appropriate to use the consent wording commonly used in that country.

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**Appendix B:**

**Excerpt from March 22, 2005 IPTF Highlights – “Follow up on MJDS and consents”:**

**Background**

Generally all information distributed in Canada should be part of the MJDS filing with the SEC. However, the MJDS forms, such as in Item 1 of Part 1 of Form F-10, state that the prospectus used in the United States need not contain any disclosure applicable solely to Canadian offerees or purchasers that would not be material to the offerees or purchasers in the United States. While the forms list several items that can be excluded it states it is not a complete list.

**Issue**

Is a company required to include the Canadian consent from its auditors in a MJDS filing with the SEC?

**Conclusion**

The Task Force noted that the inclusion of two consents has the potential to be confusing to investors and generally serves little value for U.S. investors. The Canadian consent is for Canadian investors and the U.S. consent is for U.S. investors. Therefore, the Task Force believes that registrants should not be required to include the Canadian consent in a MJDS filing with the SEC.

The SEC staff noted that many MJDS registrants were including the consent as part of the MJDS prospectus filed with the SEC. Because the offering document filed with the SEC under the MJDS is supposed to include the entire Canadian prospectus (subject to limited exceptions), this appeared to be an appropriate practice. [However, the Staff agreed to give this issue additional consideration, and respond with their final view.]

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**Discussion Document E**

**Topic: Implementation of transition for change in accountant disclosures under the SEC's Foreign Issuer Reporting Enhancements ("FIRE") rules**

**Background:**

On September 23, 2008, the SEC released its FIRE rules (the "Release")<sup>††</sup>. One of the new rules requires that foreign private issuers ("FPIs") provide disclosures about changes in their independent accountant. Because FPIs do not file Form 8-Ks and are not otherwise subject to Item 304 of Regulation S-K, the SEC will require that disclosures similar to those required by Item 304 for domestic filers be provided in a new Item 16F of Form 20-F. The disclosures required by both the resigning/dismissed independent accountant and the new independent accountant are hereinafter referred to as "change in accountant disclosures." Previously, FPIs have not been required to provide this disclosure. The "Effective Date" of the FIRE rules is December 5, 2008. The Release provides that the date which a foreign private issuer must begin to comply with the Item 16F disclosures is for its first fiscal year ending on or after December 15, 2009.

However, the text of the amendment to Form 20-F provides the following. Instruction 1 to Item 16F states that it "... applies to all annual reports and registration statements filed on Form 20-F for the issuer's fiscal years ending on or after December 15, 2009." Item 16F(a)(1) further states "if during the registrant's two most recent fiscal years or any subsequent interim period", a registrant's independent accountant resigns or is dismissed, then certain disclosures are required. Likewise, Item 16F(a)(2) indicates a similar time period and requires certain disclosures if a new independent accountant is engaged.

**Issue:**

A calendar year-end FPI files its annual report on Form 20-F for its year ended December 31, 2009 on March 15, 2010 (referred to as the 2009 Form 20-F). The FPI must comply with the amendment to provide Item 16F disclosures of Form 20-F in its 2009 Form 20-F. In the initial Form 20-F that adopts the new disclosure requirements of Item 16F, a question arises as to when must an FPI begin to comply with the change in accountant disclosure requirements. For what time period must an FPI begin to provide the change in accountants disclosures required under Item 16F?

**Discussion:**

Three alternatives appear to be the possible time periods when an FPI must begin to comply with the change in accountant disclosures.

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<sup>††</sup> See Release No. 33-8959

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View 1 – For changes in accountants for fiscal years ending on or after December 15, 2008. For the above example, the FPI should consider the period beginning January 1, 2008 when complying with Item 16F disclosure requirements in its 2009 Form 20-F.

Proponents of this view would look to Instruction 1 of Item 16F. This instruction indicates that Item 16F applies to its Form 20-F for its fiscal year 2009. The FPI then looks to Item 16F(a)(1) and (2) which state that if there was a change in independent accountant in its last two fiscal years or any subsequent interim period, then it must provide the required disclosures. Therefore, if this FPI changed its independent accountant in calendar year 2008, it would be required to provide the change in accountant disclosures on its fiscal 2009 Form 20-F annual report.

Interpretation of the disclosure requirements pursuant to this view could require an FPI to disclose changes in accountants that were made prior to both the adoption date and Effective Date of the new FIRE rules. For example, if this FPI changed its independent accountant in early 2008, implementation of the rules according to this view would require it to retroactively provide the disclosures required by the new FIRE rules adopted on September 23, 2008. Under this view, we note that FPIs may face practical challenges in complying with this rule retrospectively, e.g. in obtaining the accountant's letter.

View 2 – To comply, the FPI must consider changes in accountants occurring on or after December 5, 2008.

This possible interpretation for the time period for which the change in accountant disclosures would be provided is based on the Effective Date of the Release. While use of this date may not always be consistent with Instruction 1 to Item 16F of Form 20-F, it would provide FPIs with notice so that they could establish internal procedures to capture the information required to comply with the disclosure.

Proponents of this view would consider amendments made to Item 304 in 1988<sup>††</sup> to be analogous to the current FIRE change in accountant disclosure rules. The 1988 amendments clarified what constituted a “reportable event” and required disclosures about consultations with new accountants on accounting or auditing matters prior to their engagement. The transition specified for these amendments indicated that if the accountant change occurred after their effective date (thirty days after publication in the Federal Register in this case), then all disclosures required by the amendments were to be made even though the event or discussion being disclosed may have occurred prior to the effective date.

View 3 - For changes in accountants for fiscal years ending on or after December 15, 2009. For the above example, the FPI should consider the period beginning January 1, 2009 when complying with Item 16F disclosure requirements in its 2009 Form 20-F.

In the case of the calendar year-end FPI, this would require only those changes in accountants made in its fiscal year ended December 31, 2009 to be disclosed in its 2009 Form 20-F. Proponents of

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<sup>††</sup> See Securities Act Release No. 6766

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this view believe that this is consistent with the discussion of the “Compliance Dates” in the Release. In part, the Compliance Dates section provides that a foreign private issuer must begin to “provide disclosures pursuant to Item 16F of Form 20-F, which pertains to a change in registrant’s certifying accountant; ... for its first fiscal year ending on or after December 15, 2009.”

Furthermore, proponents of this view believe this application of the disclosure requirements in the initial Form 20-F is consistent with the following discussion in the Release:

Foreign private issuers will be required to comply with the amendments beginning with their first fiscal year ending on or after December 15, 2009. The delayed compliance date should provide these issuers and their accountants with sufficient time to establish internal procedures that will enable them to comply with the new requirements.<sup>§§</sup>

As contemplated by the above language, the calendar year-end FPI in this example may not have had the internal procedures established in 2008 to capture the information required to be disclosed.

**SEC Staff Response:**

**The Staff supports View 2. The Staff noted that a FPI must provide disclosures required by new Item 16F of Form 20-F about changes in their independent accountant for all events (that is, changes in accountants) occurring on or after December 5, 2008 in Forms 20-F for years ending after December 15, 2009. Additionally, the Staff noted that registrants electing to comply with new Item 16F of Form 20-F for periods ending prior to December 15, 2009 would need to comply with all of the applicable disclosure requirements therein.**

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<sup>§§</sup> See Release No. 33-8959, p. 53-4

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**Discussion Document F**

**Topic: Monitoring Inflation in Certain Countries**

**Background:**

At the March 2003 meeting of the Task Force, it was noted that it would be helpful to be more proactive in assessing the inflationary status of countries. As a result, it was agreed that a mechanism be developed for proactively monitoring the inflationary status of countries. That approach and the related assumptions used by the Task Force are described below:

**Approach**

The Task Force agreed to regularly consider the inflationary status of a number of countries for the purpose of determining whether they were highly inflationary as defined in FASB Statement 52. It was agreed that inflation rates be monitored regularly (monthly to the extent possible) in order to identify cases where the Task Force could discuss a country's inflationary status. Based on the cumulative inflation information, countries would be categorized as follows:

1. Countries that are clearly highly inflationary (i.e., that have cumulative inflation approaching or exceeding 100%).
2. Countries with increasing cumulative inflation rates that should be monitored.
3. Countries that are clearly not highly inflationary (i.e., with sufficiently low cumulative inflation).

**Assumptions**

The following assumptions were developed as a means of screening countries in order to determine whether the Task Force should discuss their inflationary status:

- Inflation rates used would be based on a consumer price index, unless otherwise noted. Where an index other than the CPI is used, the Task Force would need to discuss the appropriateness of the index.
- Inflation information would be derived from the "International Financial Statistics" on the IMF website. In cases where information is not provided to the IMF, local sources would be used (e.g., country central bank data).
- Countries with cumulative inflation rates not exceeding a certain level, say 70%, generally would not be considered highly inflationary based on quantitative factors alone. However, qualitative factors ultimately would be considered pursuant to EITF Topic D-55, as deemed necessary by the Task Force.
- Countries with cumulative inflation rates between 70% and 100% would be assessed for highly inflationary status given recent trends, based on the guidance in EITF Topic D-55.

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For example, in cases where the cumulative rate has declined below 100%, is that decline “other than temporary”? Or, in cases where the inflation rate has been increasing, is the cumulative rate at a level that “approximates” 100%? In addition, countries with a significant increase in inflation during the current period would be monitored.

In certain cases inflation information is not updated regularly. In such cases the following was agreed:

- Where a country was previously considered highly inflationary (i.e., the last known cumulative inflation rate previously exceeded or approached 100%), presume that still highly inflationary.
- Where a country was previously not considered highly inflationary (i.e., the last known cumulative inflation rate did not previously exceed or approach 100%), deduce the current inflation rate necessary in order to exceed 100% (the “deduced rate”). The deduced rate would be calculated solely for the purpose of determining whether or not the Task should analyze a particular country’s inflationary status. The ultimate determination of that status would depend on all relevant facts and circumstances.
  - If deduced inflation rate for the current period(s) exceeds a certain level, say 30%, then presume that not highly inflationary unless the deduced rate is consistent with the trend in recent known periods.
  - If deduced inflation rate does not exceed a certain level, say 30%, then presume highly inflationary unless the deduced rate is not consistent with the trend in recent known periods.

The Task Force agreed that qualitative factors also should be considered. The Task Force noted that the existence of objective and verifiable evidence would be necessary for a country to no longer be considered highly inflationary.

See the Appendix for detailed description of how inflation rates are determined in this analysis.

**SEC Staff Response:**

Countries considered highly inflationary

It was concluded that the following countries should be considered highly inflationary through December 31, 2008:

Myanmar  
Zimbabwe

Countries on the highly inflationary “watch list”

The following countries are on the Task Force’s inflation “watch list”:

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Ethiopia  
Guinea  
São Tomé and Príncipe  
Venezuela  
Iran

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**Appendix: Description of how inflation rates are determined**

For all countries, data is extracted from the International Monetary Fund (“IMF”) website. IMF data is extracted from [www.imf.org](http://www.imf.org) as follows:

On the home page, click the “Data and Statistics” tab, then click:

- “World Economic Outlook Databases (WEO)” link
  - Select the most recent database
    - Select “By Countries (country-level data)”
      - Select “All Countries”, then click the “continue” button.
        - Select “Inflation, end of period consumer prices”
          - Select a date range (i.e. 2004-2008); click “prepare report” and a table is produced with the data; click the “download” link to export to excel. The data table includes the end of period price indices for each country.

The IMF World Economic Outlook (“WEO”) report estimates inflation where actual inflation data has not been obtained. The text of the report describes the assumptions and conventions used for the projections in the WEO. The data that are estimated as opposed to actual are highlighted. While the IMF data has limitations (projected inflation data and varying dates through which actual data is included in the table), the calculated 3-year cumulative inflation allows us to determine which country’s calculations require further analysis.

Using the downloaded table, the 3-year cumulative inflation rate is calculated as follows (assuming the current year is 2008):

$$(2008 \text{ End of Year Index} - 2005 \text{ End of Year Index}) / 2005 \text{ End of Year Index}$$

*Countries on the “Watch List”*

For countries on the watch list, monthly inflation data (CPI) is obtained from each country’s respective central bank website. Often, that data must be manipulated because of differences in presentation or other reasons (for example, some countries have reset their base index back to 100 during recent years). Once the data has been converted to an end of period price based on a consistent index, the same calculation described above is used to calculate the 3-year cumulative inflation rate.

Using the central bank inflation data also has limitations. While it is often more current than the IMF data, each country releases its inflation data at different times. Certain countries use an Islamic calendar. Finally, some countries’ central banks do not currently publish inflation data, including some highly inflationary economies such as Zimbabwe and Myanmar.

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**III. Amendment to Discussion Document B from June, 2008 Meeting**

**Note: This paper is a reissuance of Discussion Document B from the June, 2008 meeting to include the addition of Item 4, Issue 2 and the previous Issue 2 has been renumbered as Issue 3.**

**Topic: Venezuela Exchange Controls**

**1. Background**

Pursuant to certain foreign currency exchange control regulations in Venezuela (the "Exchange Regulations"), the Central Bank of Venezuela ("BCV") centralizes the purchase and sale of foreign currency within the country. Under these regulations, the purchase and sale of foreign currency is required to be made at an official rate of exchange that is fixed from time to time by the Executive Branch and BCV (the "Official Rate"), and which currently is Bs. 2,150.00 per United States Dollar ("Dollar"). In addition to providing for exchange controls, the Exchange Regulations require the sale to the BCV, at the Official Rate, of all foreign currency received by virtue of exportation of goods, services or technology from Venezuela, and of all foreign currency that enters the country for any reason except in certain industries or other specific situations as further detailed below.

- Oil and gas companies engaged in certain qualifying activities (e.g., exploration) may retain 100% of the foreign currency collected from exportation.
- All other exporters may retain up to 10% of foreign currency collected from exportation activities to cover export costs.
- Companies selling goods or services in Venezuela, but receiving payment in foreign currency outside of Venezuela, were permitted (see recent developments section below) to retain the foreign currency outside of Venezuela. However, if such currency is brought into Venezuela or exchanged for Bolivars, it must be sold to the Foreign Exchange Administration Board (CADIVI) at the official rate or through a parallel market (as discussed below) for certain qualifying activities.

As a result of the foregoing, there has been no free market for the purchase and sale of foreign currency in Venezuela since February 2003. Although approvals for foreign currency exchanges exist they are limited. Specifically:

- Effective April 1, 2005 exports must be expressed in the currency of the destination country or in US dollars (not Bolivars) and foreign currency obtained from export operations (other than the exceptions noted above) must be sold to the BCV within 180 days.
- After proper submission and approval by the CADIVI US dollars may be acquired for imports (currently approximating US \$90 million a day) and for payment of dividends, capital gains, interest or private external debt.

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In October 2005, the Venezuelan government enacted the Criminal Exchange Law that imposes strict sanctions, criminal and economic, for the exchange of Venezuelan currency with other foreign currency through other than officially designated methods, or for obtaining foreign currency under false pretenses. The law provides for fines and penalties, including prison time in certain circumstances. However, the Criminal Exchange Law provides for an exemption for the purchase and sale of securities. The definition of securities is not explicit in the law. In practice, however, we understand that the term "securities" has come to include a) National Public Debt bonds (DPNs) denominated in Bolivars, (b) American Depository Receipts (ADRs), (c) other securities issued by Venezuela, and (d) bonds issued by Venezuela and denominated in US dollars.

The exemption for transactions in certain securities as described above has resulted in the establishment of an indirect "parallel" market of foreign currency exchange, through which companies may obtain foreign currency without resorting to or requesting it from CADIVI. The average rate of exchange in the parallel market is variable, and may differ significantly from the Official Rate. Publicly available quotes do not exist for the foreign exchange rates in this parallel market but such rates may be obtained from brokers or other means. In this market, the purchase of foreign currency is performed through a series of transactions made through a broker. For example, a company would purchase a DPN, swap it for a U.S. Dollar denominated security, sell the US Dollar denominated security on the international securities market, and obtain U.S. dollars. The swap and the subsequent sale of the US security would be performed outside of Venezuela. As such, these parallel market transactions are used to settle foreign currency obligations and to move currency in and out of Venezuela.

## **2. Previous IPTF discussion on the matter**

The Task Force has previously discussed Venezuela exchange controls at its meetings on March 4, 2003, November 25, 2003, March 9, 2004, July 27, 2004 and November 21, 2006.

A recap of certain decisions made in those meetings includes the following:

- The translation of financial statements into the reporting currency should be made at the rate that will be available for dividend remittance. Paragraph 27a of SFAS 52 requires the applicable rate at which a particular transaction could settle and the date shall be used to translate and record the transaction. Since dividends can only be remitted using the official rate, the official rate should be used. (November 21, 2006)
- The rate used for re-measurement of foreign currency denominated transactions into the functional currency depends on the type of transaction being re-measured. Since the Criminal Exchange Law, by virtue of exemption, provides for a parallel exchange mechanism and since there is an observable market rate of exchange for securities traded in this market, based on facts and circumstances this market rate may be appropriate for the re-measurement of foreign currency denominated transactions that could be settled through the parallel market mechanism. All other foreign currency transactions should be re-measured at the official rate. (November 21, 2006)
- US GAAP does not permit the use of a black market exchange rate since such a rate is not objective or determinable. Instead, individual transactions should be translated at either the parallel rate, or the official exchange rate based on the facts and circumstances, and if there are more than one official exchange rate depending on the transaction (e.g., dividend remittances), then the appropriate exchange rate should be used (March 4, 2003 - amended).

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- It would not be appropriate to deconsolidate Venezuelan operations absent any other control considerations, as the lack of exchangeability by itself does not appear to meet the "other than temporary" threshold in paragraph 26 of Statement 52 (July 27, 2004). Nor do they meet the criteria for deconsolidation as set forth in ARB 51 (November 21, 2006)
- Use of the U.S. Dollar as the functional currency would not be precluded as a result of the currency restrictions in place (July 27, 2004 meeting). The functional currency should be determined based on the specific facts and circumstances and the criteria in Statement 52. (November 21, 2006)
- The rate used for re-measurement purposes or translation of financial statements may not be reflective of economic reality and additional disclosure may be necessary (e.g., summarized financial information of Venezuelan operations in a footnote; disclosure of exchange rate used; disclosure of the net monetary assets and liabilities by currency; discussion of potential impact of a change in exchange rates on financial statements in MD&A) (March 4, 2003).

**3. Recent Developments:**

On December 28, 2007, the Venezuelan Government published an amendment to the Criminal Exchange Law that became effective on January 27, 2008. Such amendment, among other changes, established that firms or individuals, who offer, advertise or divulge financial or stock exchange information in written, audiovisual, radio-electric or any other form, regarding the quoted prices for foreign exchange, other than the official rate, will be fined 1,000 tax units for the first violation, and 2,000 tax units per subsequent violation. We understand that as a result of this amendment, brokers no longer publish the implicit parallel market exchange rates. However, prices for the purchase and sale of the underlying bonds are still available from brokers. We understand that the purchase and sale of U.S. Dollar denominated securities is still legal in Venezuela and is an accepted method of converting Bolivars to US Dollars. Further, we understand that the amendment had the following impacts:

- it is now illegal to offer, advertise or divulge financial or stock exchange information regarding the quoted prices for foreign exchange rates other than the Official Rate;
- for companies offering goods and/or services for purchase, sale or lease in Venezuela, any such offer, whether public or private, denominated in currencies other than the Bolivar are prohibited;
- as a result of this amendment to the Criminal Exchange Law, there is no longer any public information about trading volumes; and
- as a result of the amendment to the Criminal Exchange Law, quotations may vary more widely among financial institutions and brokers due to the increase in the volatility of this type of transaction and lack of public information regarding rates.

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#### **4. Issues**

The question has been raised as to whether the recent amendment to the Criminal Exchange Law as described above impacts the Task Force's prior conclusions on Venezuelan currency issues. These issues include 1) whether foreign exchange restrictions in Venezuela are so severe that they potentially cast significant doubt on an entity's ability to control (and therefore consolidate) a Venezuelan subsidiary and, 2) which exchange rate should be used to re-measure transactions and translate financial statements of Venezuelan companies. The Task Force's consideration of these issues is as follows:

##### **Issue 1:**

**Since restrictions regarding exchangeability have remained in place for almost six years and there is no indication that the restrictions will be removed, and in fact enforcement of the restrictions has been enhanced, should companies continue to consolidate Venezuelan subsidiaries?**

##### **Task Force Recommendation:**

The Task Force continues to believe that exchangeability restrictions in Venezuela are not so severe as to represent a "lack of exchangeability" under Statement 52. Nor does the Task Force believe that they meet the criteria for deconsolidation as set forth in ARB 51.

However, consistent with its prior discussions on this issue, the Task Force believes that additional restrictions on a parent company's ability to control the subsidiary entity should be carefully considered. In circumstances where exchange controls exist, other regulations or conditions could be present that impact the parent company's control over the operations of the subsidiary. If other conditions are present, they should be evaluated on a facts and circumstances basis, together with the exchange controls, to determine whether sufficient control exists to support consolidation.

##### **SEC Staff Response:**

**The staff agrees with the Task Force's view.**

##### **Issue 2:**

**Question: Is it appropriate to use the parallel market rate for purposes of foreign currency remeasurement under FAS 52?**

Paragraph 27a of SFAS 52 indicates that the applicable rate at which a particular transaction could be settled at the transaction date should be used to translate and record the transaction. A registrant's determination of whether the Amendment to the Criminal Exchange Law has changed the ability to access the parallel market should be made by its management in consultation with legal counsel, if necessary.

If the parallel market is determined to still be a readily available means by which U.S. dollar denominated transactions can be settled, then the following view outlined in the discussion of Issue 2 of Document E of the Task Force meeting of November 21, 2006 should continue to be followed.

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...[T]he rate used for re-measurement of foreign currency denominated transactions into the functional currency depends on the type of transaction being re-measured. Since the Criminal Exchange Law, by virtue of exemption, provides for a parallel exchange mechanism and since there is an observable market rate of exchange for securities traded in this market, based on facts and circumstances this market rate may be appropriate for the re-measurement of foreign currency denominated transactions that could be settled through the parallel market mechanism. All other foreign currency transactions should be re-measured at the official rate.

Whatever rate is used for re-measurement purposes or translation of financial statements may not be reflective of economic reality and additional disclosure may be necessary. Potential relevant disclosures would include summarized financial information of Venezuelan operations; disclosure of exchange rate used; disclosure of the net monetary assets and liabilities by currency (e.g., Bolivars, US dollars, etc.); and discussion in MD&A of potential impact of a change in exchange rates on financial statements.

If it is determined that the parallel market is not a readily available means by which U.S. dollar denominated transactions can be settled, then the official rate should be used for all U.S. dollar denominated transactions.

**SEC Staff Response:**

**The staff agrees with the Task Force's view.**

**Issue 3:**

**Is it appropriate to use the parallel market rate for purposes of foreign currency translation under FAS 52?**

View A: Paragraph 27b of SFAS 52 indicates that "In the absence of unusual circumstances, the rate applicable to conversion of a currency for purposes of dividend remittances shall be used to translate foreign currency statements." The existence of the parallel market does not constitute unusual circumstances potentially justifying the use of an exchange rate other than the Official Rate for purposes of foreign currency translation. Further, footnote 4 in SFAS 52 clearly contemplates that unsettled transactions may be subject to and translated using preference or penalty rates, while translation of foreign currency statements is based on the rate applicable to dividend remittances, and establishes a mechanism for reconciling differences arising from such translation relating to intercompany receivables and payables. As a result, it would appear to be appropriate to continue to use the Official Rate applicable to conversion of currency for purpose of dividend remittances to translate foreign currency financial statements.

View B: While footnote 4 in SFAS 52 clearly contemplates that unsettled transactions may be subject to and translated using preference or penalty rates, while translation of foreign currency statements is based on the rate applicable to dividend remittances, it establishes a mechanism for reconciling differences arising from such translation relating to intercompany receivables and payables, but does not contemplate the anomalies that may result from using different rates for translation and remeasurement of foreign currency transactions with third parties. Further, in its July 12, 1983 Status Report, the FASB noted that "issues involving multiple exchange rate systems are primarily questions of fact and the underlying facts and circumstances must be considered in evaluating the validity of exchange rate. As a result, companies should

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consider whether the existence of the parallel market constitutes "unusual circumstances", as contemplated in paragraph 27.b. which might warrant use of parallel market rates for purposes of foreign currency translation based on their specific facts and circumstances.

**Task Force Recommendation:**

View A

**The staff agrees with the Task Force's view.**

**5. Examples**

The following examples are provided for discussion purposes only and illustrate application of the above views to determine which exchange rate should be used for re-measurement and to translate Bolivar denominated financial statements into the Reporting Currency:

**Example 1**

A US multinational company with a wholly-owned subsidiary in Venezuela. The functional currency of the subsidiary is the Bolivar. The subsidiary purchases inventory from its parent in US Dollars creating a US Dollar denominated inter-company payable. The subsidiary's reporting currency is the US Dollar. The company determines that the parallel market is still a readily available means by which U.S. dollar denominated transactions can be settled and believes that it is probable that they will settle the inter-company payable at the parallel rate. Historically, the Subsidiary has been able to remit dividends to its US parent at the official exchange rate.

The subsidiary should re-measure its US Dollar inter-company payable at the parallel market exchange rate and translate its financial statements into US Dollars at the official rate. Any difference created between inter-company receivable and payables should be treated as a receivable or payable in the enterprise's financial statements, until the difference is eliminated by settlement, in accordance with Footnote 4 of paragraph 27.b. of SFAS No 52.

**Example 2**

A US multinational with a subsidiary in Venezuela. The functional currency of the subsidiary is the Bolivar. The subsidiary has an investment in USD denominated securities, considered to be debt securities under SFAS No. 115. The securities have been designated as Available For Sale. The company determines that the parallel market is still a readily available means by which U.S. dollar denominated transactions can be settled. If sold, it is probable that the investment securities would be sold in the parallel market. In addition, the subsidiary holds cash denominated in US Dollars in a financial institution outside of Venezuela. If converted to Bolivar, it is probable that the transaction would be settled at the parallel market exchange rate. The subsidiary originally purchased the US Dollar denominated securities and the US Dollar cash at the parallel market exchange rate in order to economically hedge further devaluation of the Bolivar at parallel market rates. The Subsidiary has historically remitted dividends to its parent at the official exchange rate.

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The subsidiary should re-measure the investment securities and the cash at the parallel market exchange rate. The subsidiary should translate the securities and cash, as well as the remainder of its net assets, at the official rate, because this is the rate that is available for dividend remittances.