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DEAR CENTER MEMBERS

SEC Issues Staff Paper Exploring a Possible Method for Incorporating IFRS

On May 26, 2011, the Office of the Chief Accountant of the Securities and Exchange Commission (SEC or Commission) issued a Staff Paper seeking feedback on a possible method of incorporating international financial reporting standards (IFRS) as issued by the International Accounting Standards Board (IASB) into the U.S. financial reporting system. The method discussed in the Staff Paper was first introduced by the SEC's Deputy Chief Accountant, Paul Beswick, at the December 2010 AICPA National Conference on SEC and PCAOB Developments and was referred to as a "condorsement" approach (the framework). Comments are due by July 31, 2011.

The Staff Paper makes clear that the Commission has not yet made a decision as to whether and, if so, how, to incorporate IFRS into the financial reporting system for U. S. issuers. The focus of the Staff Paper is to outline a possible approach for incorporating IFRS into the U.S financial reporting system, as the SEC staff continues to work on the Work Plan as described in the commission Statement in Support of Convergence and Global Accounting Standards.

What is the Framework?

In performing their analysis of how other jurisdictions incorporate IFRS into their reporting systems, the SEC Staff have identified two different approaches to incorporation: 1) countries that converge their local standards with IFRS without a firm commitment to incorporate fully IFRS as issued by the IASB, called the "Convergence Approach"; and 2) countries that use IFRS after some form of a national or multinational incorporation process – that is, they undertake some form of local endorsement - called the "Endorsement Approach."

In this Staff Paper, the SEC has suggested another possible incorporation approach, which they refer to as the "condorsement" approach. This approach to incorporation combines elements of both the Endorsement Approach as well as the Convergence Approach. More specifically, this approach would consist of the Endorsement Approach that would share characteristics of the incorporation approaches with other jurisdictions that have incorporated or are incorporating IFRS into their financial reporting systems. However, during the transitional period, the framework would employ aspects of the Convergence Approach to address existing differences between IFRS and U.S. GAAP. This framework would retain a U.S. standard setter – the Financial Accounting Standards Board (FASB).

What would the FASB's and SEC's Role be?

The SEC Staff believes it will be important for the United States to continue to have an active role in the international accounting arena for the following reasons: 1) to assist in the development and promotion of high quality, globally accepted accounting standards; 2) to be proactive in identifying new and emerging financial reporting issues; and 3) to ensure that U. S. interests are suitably addressed in the development of those standards. The SEC Staff believes that the FASB would be the existing body best equipped to fulfill this role within the U.S. and is already positioned to do so.

Under the endorsement aspect of the framework, the FASB would continue to participate in the development and improvement of accounting standards, however, the manner of participation would differ considerably from the FASB's current standard-setting role. The most significant difference is that the FASB would participate in the process for developing IFRS, rather than serving as the principal body responsible for developing new accounting standards or modifying existing standards under U.S. GAAP. In other words, the FASB would continue to promulgate U.S. GAAP primarily through its endorsement of standards promulgated by the IASB while retaining the authority to modify or add to the requirements of the IFRSs incorporated into U.S. GAAP subject to an established incorporation protocol. The Staff Paper states that modifications or additions to the requirements of IFRSs under this approach should be rare and generally avoidable with the objective that U.S. GAAP remains consistent with IFRS as issued by the IASB. In addition, the FASB would serve as an educational resource for U.S. constituents to facilitate the understanding and proper application of IFRS.

With regard to the SEC, the Commission would maintain its oversight over the FASB as the designated U.S. national standard setter, with a less direct oversight relationship with the IASB. However, the SEC would be actively engaged in the standard-setting process and with the broader activities of the IASB and its governance bodies. Many of the SEC's activities would remain similar to those performed currently, while other activities and interactions with the IASB and its staff would develop over time.

How Will the Transition to IFRS Occur?

The Staff Paper indicates that the transition to IFRS would potentially consist of a multi-step process that would be completed over a period of several years – i.e., five to seven years. Transition to IFRS would involve the replacement of the content of existing U.S. GAAP with the content of IFRS as issued by the IASB. If the Commission decides to pursue this framework, the FASB would need to develop a transition plan in a relatively short period to allow for U.S. constituents to plan appropriately. FASB's transition plan would consist of evaluating IFRSs individually in order to determine: 1) how and when to incorporate the standards into U.S. GAAP during the transition period; and 2) whether the incorporation should be staged, phased or occur all at once. The Staff Paper describes a possible approach to address the initial incorporation that organizes the IFRSs into three difference categories: 1) IFRSs subject to MoU projects; 2) IFRSs included on the IASB's current standard-setting agenda; and 3) All other existing IFRSs, and areas not addressed by IFRSs.

What are the Benefits and Risks of the Framework?

The Staff Paper elaborates on the following potential benefits and risks of the framework that are being contemplated. The Staff will continue to identify and analyze other potential benefits and risks of the framework, as compared to other possible incorporation approaches, as the Commission contemplates a decision in determining whether and, if so, how, to incorporate IFRS into the U.S. financial reporting system.

- Supports a flexible, tailored transition strategy;
- Provides for gradual implementation;
- Potentially greater investor protection with FASB endorsement than direct incorporation of IFRS; and
- Retains "U.S. GAAP" as the statutory basis for financial reporting.

SEC's Request for Comment on the Staff Paper

The SEC Staff is interested in constituent's feedback regarding the framework and any other possible approaches of incorporation of IFRS, including views on those approaches explored previously. Feedback is requested to be received by the SEC by July 31, 2011. All comments can be submitted to the SEC by clicking here.

SEC Roundtable Scheduled for July 7, 2011

The SEC also plans to sponsor a roundtable on July 7, 2011 to discuss benefits and challenges in potentially incorporating International Financial Reporting Standards (IFRS) into the financial reporting system for U.S. issuers. This roundtable, which will feature three panels representing investors, smaller public companies, and regulators, will focus on topics such as investor understanding of IFRS and the impact on smaller public companies and on the regulatory environment of incorporating IFRS.

Please note that this summary is intended as general information and should not be relied upon as being definitive or all inclusive. The CAQ encourages member firms to refer to the Staff Paper in its entirety at the hyperlink provided above.

Other Related Resources:

Global Accounting Standards	SEC's Spotlight on Work Plan for Global Accounting Standards
CAQ Alert 2010-64	SEC Publishes Progress Report on Work Plan for Global Accounting Standards, November 8, 2010
CAQ Guide to IFRS	CAQ Guide to IFRS provides interested parties with useful information to facilitate public discussion among all stakeholders, September 2009

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