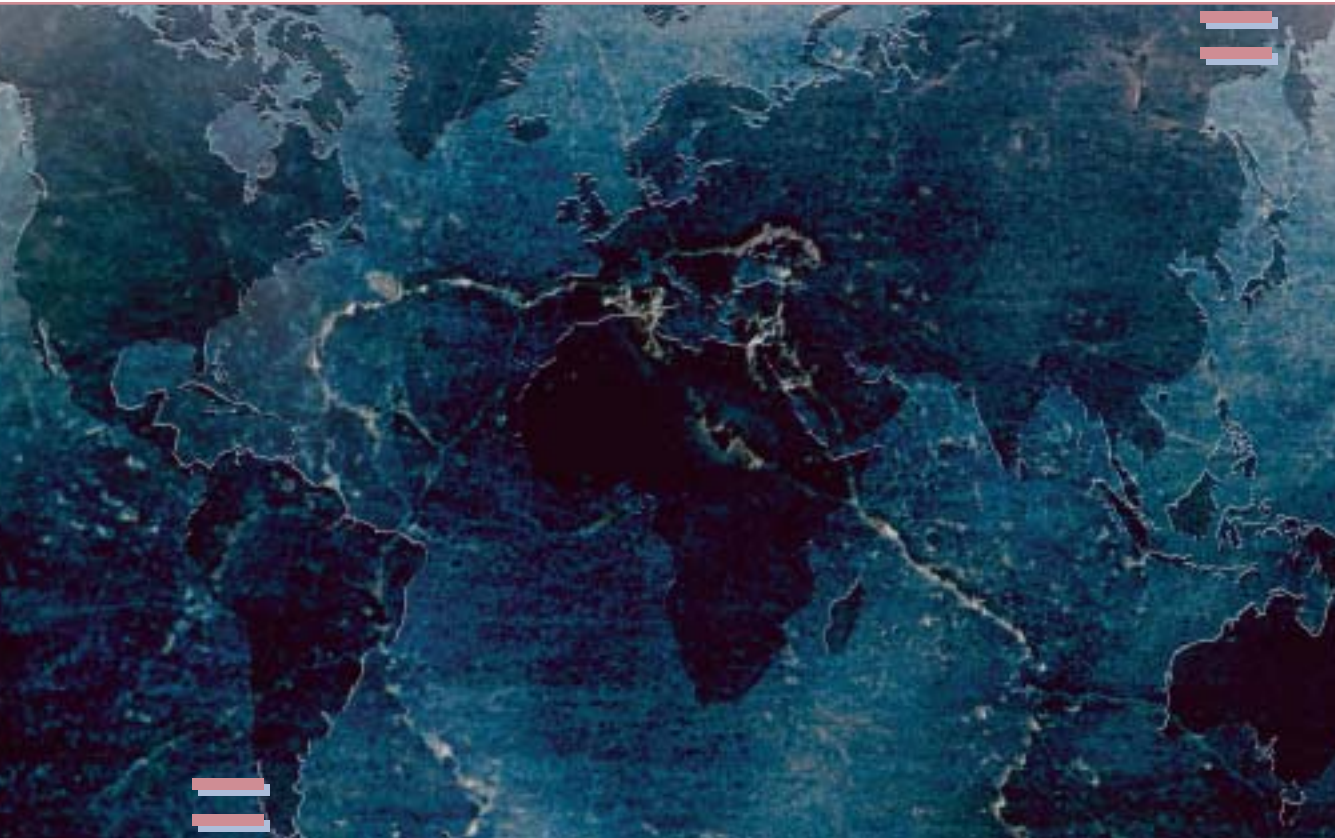


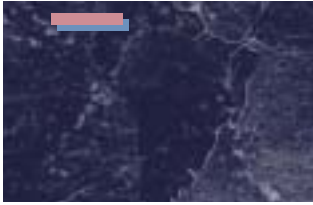
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CHALLENGES AND SUCCESSES IN  
IMPLEMENTING INTERNATIONAL STANDARDS:  
ACHIEVING CONVERGENCE TO IFRSs AND ISAs

# INTRODUCTION

BY PETER WONG



Peter Wong, a former member of the Board of the International Federation of Accountants (IFAC), was commissioned by IFAC to study the challenges and successes in adopting and implementing international standards.

A financial reporting system supported by strong governance, high quality standards, and sound regulatory frameworks is key to economic development. Indeed, high quality standards of financial reporting, auditing, and ethics underpin the trust that investors place in financial and nonfinancial information and, thus, play an integral role in contributing to a country's economic growth and financial stability.

As the forces of globalization prompt more and more countries to open their doors to foreign investment and as businesses themselves expand across borders, both the public and private sectors are increasingly recognizing the benefits of having a commonly understood financial reporting framework supported by strong

globally accepted auditing standards.

The benefits of a global financial reporting framework are numerous and include:

- Greater comparability of financial information for investors;
- Greater willingness on the part of investors to invest across borders;
- Lower cost of capital;
- More efficient allocation of resources; and
- Higher economic growth.

Before these benefits can be fully realized, however, there must be greater convergence to one set of globally accepted high quality standards. International convergence is a goal that is embraced in IFAC's mission, shared by IFAC member bodies, the international standard setters, and many national standard setters, and supported by international regulators. Achieving international convergence, however, requires more than theoretical support. It requires reaching consensus as to the international standards that will

serve as the foundation for financial reporting and auditing globally, determining how to facilitate the adoption of those standards, and, ultimately, taking the actions necessary to encourage implementation. This report is a significant step in that process.

In November 2003, the IFAC Board agreed that there was a need to identify more clearly the challenges to adopting the international standards and to communicate successful examples of how the international standards have been and are being implemented. As a former IFAC Board member, past president of the Hong Kong Institute of Certified Public Accountants, and a Chartered Accountant who has worked with both national and international standards for many years, I was asked to lead this project.

The project, defined in more detail on page 4, entailed the collection of views from a cross-section of the international financial reporting community: representatives from regional and national professional accountancy organizations; IFAC committees and permanent task forces; national standard setters; users of financial statements; regulators; and professional accountants from a variety of backgrounds.

This report details my findings and proposed actions for addressing the identified challenges.

The objective of this report is to stimulate further discussions and actions on the adoption and implementation of the international standards so that we

may move closer to the goal of international convergence. Based on the successes of adoption and implementation in some countries, I believe it is a goal that is achievable over time. Given the significant public interest benefits, it is also a goal that I believe we cannot afford to put aside.

Serving the public interest is one of the greatest challenges facing our profession. To do so effectively,

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**THE** *objective of this report is to stimulate further discussions and actions on the adoption and implementation of international standards so that we may move closer to the goal of international convergence.*

we must all demonstrate that we follow high professional standards. The public will not and should not accept anything less. If there are any impediments to our ability to follow professional standards,

IFAC, together with international and national standard setters, regulators, governments, and others identified in this report, must work together to address them head-on.

I am grateful for the help of the regional and national professional accountancy organizations that assisted in the arrangement of discussion groups, for those who took the time to participate in the discussions or to complete written submissions, and for the dedication of the IFAC staff in supporting me in this project.

Finally, I must state that the views in this report are my personal views and do not necessarily reflect the views of any of the organizations with which I am affiliated.



**PETER H.Y. WONG**

Peter Wong was a member of the Board of the International Federation of Accountants from 2000 to 2003 and is currently a member of the Board of the Global Reporting Initiative, which sets the Guidelines for Sustainability (Environment, Social & Economic) Reporting. He retired as Senior Tax Partner of Deloitte Touche Tohmatsu – Hong Kong in May 2002 and is currently a consultant to the firm. A past president of the Hong Kong Institute of Certified Public Accountants, he is now the chairman of the Business & Professionals Federation of Hong Kong.

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## BACKGROUND



As the world continues to globalize, discussion of convergence of national and international standards has increased significantly. Most major capital markets are now actively discussing or pursuing efforts of convergence towards single sets of globally accepted accounting and auditing standards. IFAC, in an effort to facilitate international convergence, commissioned this study to explore the challenges and successes involved in adopting and implementing international standards. It is joined by international regulators, including the Basel Committee on Banking Supervision, the European Commission, the Financial Stability Forum, the International Association of Insurance Supervisors, the International Organization of Securities Commissions, and the World Bank, in recognizing that global capital markets require high quality, globally consistent, and uniform regulatory and standards regimes.

### *The Benefits of Globally Accepted International Standards*

Globally consistent and uniform financial systems provide cost-efficiencies to business and greater safeguards to the public. The public is entitled to have confidence that, regardless of where a business activity occurs, the same high quality standards were applied. It is widely recognized that investors will be more willing to diversify their investments across borders if they are able to rely on financial information based on a similar set of standards. Thus, adherence to international standards, such as those developed by the International Accounting Standards Board (IASB) and the International Auditing and Assurance Standards Board (IAASB), can ultimately lead to greater economic expansion.

### *Support for International Convergence*

The Financial Stability Forum (FSF)<sup>1</sup> included the International Financial Reporting Standards (IFRSs) issued by the IASB and the International Standards on Auditing (ISAs) issued by the IAASB in its *12 Key Standards for Sound Financial Systems*. The FSF indicated that these 12 Key Standards are most likely to make the greatest

contribution to reducing vulnerabilities and strengthening the resilience of financial systems.

The report on *Rebuilding Public Confidence in Financial Reporting – An International Perspective*, issued in July 2003, provided further support for IFRSs and ISAs becoming the worldwide standards. The report was developed by the Task Force on Rebuilding Public Confidence in Financial Reporting – an independent group commissioned by IFAC to address, from an international perspective, the loss of credibility in financial reporting and approaches to resolving the problem. The task force recommended that convergence of national and international standards be achieved as soon as possible, viewing this as a significant public interest issue.

IFAC has committed itself to the achievement of global convergence of national standards with IFRSs and ISAs. This is evidenced both in its mission statement and in its Statements of Membership Obligations. Published in April 2004, the Statements of Membership Obligations formally capture IFAC's longstanding requirement that its member bodies support the work of the IASB and IAASB by using their best endeavors to incorporate the IFRSs and ISAs in their national requirements (or where the responsibility for the development of national standards lies with third parties, to persuade them on a best endeavors basis to do so) and to assist with the implementation of IFRSs and ISAs, or national standards that incorporate IFRSs and ISAs.

As countries increasingly commit to converging national standards with IFRSs and ISAs, there is a need to ensure international convergence is approached in a systematic and, where possible, consistent way across jurisdictions. It also has made it necessary for interested parties, such as IFAC, the international and national standard setters, and international regulators, to understand the challenges in adopting and implementing the international standards so that they can be addressed at an early stage.

### *Scope and Project Methodology*

This study seeks to explore those issues that affect the adoption and implementation of IFRSs and ISAs, provides examples of successful adoption and implementation to serve as models for other countries, and proposes actions to be taken by relevant stakeholders.

Numerous questions were addressed as part of this study. How do we move towards international convergence? What obstacles need to be overcome? What systems

<sup>1</sup> The FSF is an organization that brings together senior financial representatives of national financial authorities, international financial institutions, international regulatory and supervisory groupings, committees of central bank experts, and the European Central Bank to promote international financial stability.

and processes can help to facilitate international convergence? What roles can the IASB and IAASB and national standard setters play in ensuring that international convergence is approached in a systematic and, where possible, consistent way? This report attempts to answer these questions based on input from a cross-section of the international financial reporting community.

Peter Wong, a former IFAC Board member with extensive international experience, was appointed by the IFAC Board to oversee the development of this study and address these questions among a variety of groups: those that develop the international and national standards, those that use the standards, and those that rely on work performed based on the standards.

The major fact-gathering process was as follows:

- A series of focus group meetings with members of regional and national professional accountancy organizations;
- A series of interviews with representatives of national standard setters, preparers, auditors, and users of financial statements, including regulators, and other interested parties;
- An invitation to IFAC member bodies to submit written responses; and
- Limited library research, focused on recent studies undertaken with regard to the adoption and implementation of the international standards.

Nine focus group meetings were held, approximately 20 interviews were conducted, and 29 responses to the invitation were submitted to IFAC. Those who participated in focus groups or interviews or submitted written responses are hereinafter referred to as “participants” in this study. The participants represented a broad range of perspectives – regulators, standard setters, preparers from entities of various sizes, auditors from large and small accounting firms, and investment professionals – and shared a combination of organization-wide and personal views.

Appendix 1 contains a list of focus groups, interviews, and respondents to the invitation to submit written responses. Appendix 2 contains a list of questions covered in these meetings, interviews, and the invitation to submit written responses.

Peter Wong, with the assistance of senior IFAC staff members, engaged in discussions regarding the following potential challenges in adopting and implementing the international standards:

- Issues of incentives – the various factors which might encourage or discourage national decision-makers from their adoption.
- Issues of regulation – regulatory challenges in their adoption.
- Issues of culture – challenges arising from cultural barriers in their adoption and implementation.
- Issues of scale – implementation barriers associated with the relative costs of compliance for small- and medium-sized entities and accounting firms.
- Issues of understandability – their complexity and structure.
- Issues of translation – the ease of their translation and the resources available to undertake the translation.
- Issues of education – the education and training of students and professional accountants in the international standards.

Subsumed in the above are issues related to the legitimacy and authority of the international standards and the integrity of those who have to implement them, i.e., to comply with the substance and form of the standards.

These challenges are explored throughout this report. The report also reflects reported successes in adopting and implementing the international standards. As more countries seek to adopt the international standards, experiences from those countries already well advanced in their adoption and implementation are of immense value to those that are still in the process, or are considering the steps to be taken.

The evidence contained in this report is anecdotal, as opposed to quantitative. Given the diversity of groups involved in the study and the consistency in responses, the study provides a clear indication of the challenges to be addressed to facilitate the adoption and implementation of the international standards.

It should be noted that the project focused on the adoption and implementation of IFRSs and ISAs. Where participants noted matters relating to the pronouncements issued by IFAC committees other than the IAASB, for example, matters relating to ethics, education, or financial reporting in the public sector, these matters have been communicated to the relevant committee. □

## SUMMARY OF PRINCIPAL FINDINGS AND BASIC ASSUMPTIONS



Generally, participants were positive about the adoption and implementation of the international standards and confirmed that the IASB and the IAASB were the appropriate bodies

to develop them.

Participants cited similar challenges related to the adoption and implementation of both IFRSs and ISAs. They were inclined to spend more time, however, discussing the international accounting standards than the international auditing standards. A participant (from industry) gave the following explanation for this:

*“The international accounting standards have a direct effect on far more people than the international auditing standards. The complexity of the international auditing standards might flow through into the audit fee an entity pays, but the entity does not itself have to read, interpret, and implement the standards.”*

The principal challenges identified by those involved in adopting and implementing IFRSs and ISAs are described in the following sections of this report:

- Understanding the Meaning of International Convergence
- Translation of the International Standards
- Complexity and Structure of the International Standards
- Frequency, Volume, and Complexity of Changes to the International Standards
- Challenges for Small- and Medium-sized Entities and Accounting Firms
- Potential Knowledge Shortfall
- Implications of Endorsement of IFRSs

This report explores these challenges in detail and includes success factors demonstrating how some countries and organizations have addressed or overcome some of the challenges. Additionally, proposed actions that are based on an analysis of the findings and participants’ recommendations are included for each of the

challenges. A list of proposed actions by each stakeholder group is featured at the end of the report. Although not agreed or endorsed by any formal group of IFAC or any other international organization, these proposed actions have been developed to further the goal of international convergence.

The proposed actions are premised on the following:

- Successful adoption of the international standards is dependent on the development of high quality standards.
- Integrity in the application of the international standards is essential. Preparers, auditors, and users of financial statements must encourage and support compliance with the substance and form

of the international standards.

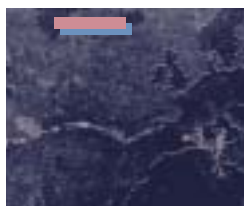
- The adoption and implementation of the international standards require action at both the national and international levels. At the national level, it is important that governments, regulators, and national

standard setters place international convergence as a priority on their agendas. At the international level, it is important that the international standard setters establish processes and procedures that facilitate national input and lead to the development of high quality standards that are globally accepted.

Finally, it is clear that to achieve international convergence, action is necessary at all points along the information supply chain that delivers financial reporting. Boards of directors and management, who have the primary responsibility for financial reporting, as well as auditors, standard setters, regulators, and other participants in the financial reporting process, such as lawyers, investment bankers, analysts, credit rating agencies, and educators, all have important roles to play in achieving international convergence. □

**TO** achieve international convergence, action is necessary at all points along the information supply chain that delivers financial reporting.

## UNDERSTANDING THE MEANING OF INTERNATIONAL CONVERGENCE



### What Does “Adoption” Mean?

The question, “*To what degree do you consider that the international standards have been adopted in your country?*” gave rise to varied responses largely because there was no universally accepted definition of “adoption.” Participants referred to “adoption,” “harmonization,” “transformation,” etc. without clearly defining what those terms meant. For example, what does it mean to be “largely harmonized?” One written submission noted that the national standards have been “based on” the international standards, and that the national accounting standards are at least 80% identical to IFRSs and the national auditing standards are at least 95% identical to ISAs. International convergence is a process, with adoption as the end result. However, without a universally accepted definition of “adoption,” it is difficult to measure progress towards international convergence.

The World Bank, in preparing the *Reports on the Observance of Standards and Codes*, encountered similar diversity regarding the concept of adoption. It found that the adoption of IFRSs could be categorized as: full adoption of IFRSs; full adoption of IFRSs, but with time lag; selective adoption of IFRSs; and national standards “based on” IFRSs. The adoption of ISAs could be categorized similarly, but with one addition: adoption of a summarized version of the ISAs. Furthermore, in all the ISA categories the adopted ISAs may contain additional national requirements.

The time lag in adopting the international standards is due mainly to translation of the standards. For example, in one country a five-year time lag was experienced due to the need for translation of the ISAs.

Selective adoption of the international standards is due mainly to the complexity of the standards, the incompatibility thereof with national culture, or potential implementation problems. For example, in one country the ISAs were summarized in 33 pages, as the complete standards were felt to be “over-

whelming.” The implementation of these summarized ISAs was intended to be a first step to full adoption; however, that country is now in the sixth year of this temporary stage.

According to paragraph 14 of International Accounting Standard 1, *Presentation of Financial Statements*, financial statements shall not be prescribed as complying with IFRSs unless they comply with all the requirements of IFRSs. Paragraph 53 of the exposure draft of the proposed revised ISA 700, *The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements*, states that the auditor’s report should only refer to the audit having been conducted in accordance with ISAs when the auditor has complied fully with all of the ISAs relevant to the audit. This leaves the preparers and auditors of financial statements in countries that have not fully incorporated the IFRSs and ISAs in their national standards with a dilemma. Although the national standards have been developed with reference to the international standards, they may not fully incorporate them and, consequently, the financial statements and auditor’s report should not refer to compliance with IFRSs and ISAs.

Furthermore, a reference to national standards that are “materially the same” or “substantially the same” as IFRSs or ISAs is confusing and potentially misleading.

### A MODEL OF CONVERGENCE

In March 2004, the Accounting Standards Board (ASB) in the United Kingdom issued a discussion paper, *UK Accounting Standards: A Strategy for Convergence with IFRS*. The paper sets out the ASB’s views on the future development of national accounting standards. Specifically, it states that the ASB believes that there can be no case for the use in the United Kingdom of two sets of wholly different accounting standards in the medium term, and it should not seek to issue new standards that are more demanding or restrictive than IFRSs. These propositions require a concerted effort from the ASB to bring national accounting standards into line with IFRSs. The ASB intends to achieve this as quickly as possible while avoiding the burden of excessive changes in any one year and, in particular, minimizing the cases in which an entity using national accounting standards may be required to make successive changes of accounting policy in respect of the same matter.



### *Amendments for National Specificities*

The adoption and implementation of the international standards in a country takes place in an environment that is affected by factors unique to that country, for example, the economy, politics, laws and regulations, and culture. A reason cited by participants for not fully incorporating IFRSs and ISAs is that countries find it necessary to amend the international standards to provide for national specificities. Projects undertaken by the Fédération des Experts Comptables Européens (FEE), the Auditing Practices Board (APB) in the United Kingdom, and the Australian Accounting Standards Board (AASB) further confirm this situation.

In March 2004, FEE issued a paper on *ISA+ in the EU: A Summary of Country-Specific Audit Requirements*, which categorizes additional national requirements as: additional explicit reporting required by law or regulation; additional exception reporting required by law or regulation; additional reporting required by national auditing standards; and significant additional procedures required by national auditing standards. National law, regulation, and auditing standards gave rise to many divergences from ISA 700, *The Auditor's Report on Financial Statements*. In addition, 11 of the 30 countries included in the summary identified one or more significant procedures not contained in the ISAs.

In June 2004, the APB issued an exposure draft on proposed *International Standards on Auditing (UK and Ireland)*. The APB is proposing to revise the existing national auditing standards to ensure that they, at a minimum, meet the requirements of the ISAs. In developing the exposure draft, the APB reviewed all the national standards to identify differences between the national standards and ISAs. Where identified differences were considered to be relevant and helpful, such material was incorporated in the ISAs for application in the United Kingdom.

The AASB has adopted the IFRSs with minimum amendments to accommodate national laws and regulations, eliminate some options, make the standards private and public sector neutral, make conforming amendments to the terminology in some of the IFRSs that have not recently been revised, and retain a small amount of guidance that is in the existing AASB standards.

Similarly, many other countries are finding it necessary to incorporate national legal and regulatory requirements and national practice in their adopted international standards or to eliminate international requirements because of “legal obstacles.” In the future, however, this practice may no longer be acceptable.

In accordance with the European Commission's *Proposal for a Directive of the European Parliament and of the Council on Statutory Audit of Annual Accounts and Consolidated Accounts and Amending Council*

*Directives 78/660/EEC and 83/349/EEC* (March 16, 2004), European Union (EU) member states will be allowed to impose additional audit procedures only if these follow from specific requirements relating to the scope of the statutory audit. Furthermore, EU

member states will have to communicate these additional procedures to the Commission.

In addition to national specificities such as national laws, regulations, and practice, the tax-driven nature of the national accounting regime was also identified as a barrier to international convergence. For example, in some countries one of the primary objectives of the national accounting standards traditionally has been to determine taxable income. Financial statements prepared in accordance with IFRSs are intended primarily to serve the needs of the capital markets, which may differ significantly from the needs of the tax authorities.

**SIMILARLY**, many other countries are finding it necessary to incorporate national legal and regulatory requirements and national practice in their adopted international standards.

### *Date of International Convergence and Effective Dates of Adopted International Standards*

In some instances, participants reported that their countries have adopted the international standards in issue at a particular date, but have not kept up-to-date with new and revised international standards issued subsequent to that date.

In other instances, it was found that the national standards have different effective dates and transitional provisions from those of the international standards on which they are based.

This leaves the preparers and auditors of financial statements in the same dilemma as discussed earlier. Any reference to compliance with the international standards should be made only if there was full compliance with all the international standards effective at that date.

### *Accessibility to the International Standards*

Limited accessibility to some or parts of the international standards was identified as a barrier to international convergence. Some participants, particularly those from developing countries, were concerned that fees are being charged to obtain the IFRSs. Similarly, participants from the EU, who will have free-of-charge access to parts of the IASB literature, were concerned that guidance essential for proper implementation of IFRSs would not be available free of charge and, as a result, might not be considered by entities implementing IFRSs.

### *Conclusions and Proposed Actions*

It is evident that international convergence is a process. This process could be enhanced by IFAC through greater clarification of the end result, i.e., the meaning of “adoption,” and by the development of a more consistent and globally recognized measurement of international convergence. While consideration needs to be given as to how best to accommodate national laws and regulations, greater consistency in approach by those adopting the international standards is needed. Governments and regulators are encouraged to establish legal and regulatory environments that provide for compliance with the international standards, with no or very limited additional national requirements. Governments are also encouraged to acknowledge the differing roles of tax accounting and financial reporting.

National standard setters are encouraged to make international convergence the core of their work and the focus of their resources, and to interface with the international standard setters on behalf of their national constituencies. International standard setters need to continue to recognize the unique challenges faced by national standard setters and to provide sufficient opportunity for national standard setters to provide input to the international standard-setting processes. Of note is the joint effort by the Financial Accounting Standards Board (FASB) in the United States and the IASB to eliminate differences between the national accounting

## SUCCESS FACTORS

Factors that contributed to national standard setters’ success in adopting and implementing the international standards include:

- The development of and commitment of all stakeholders to a formal international convergence policy that clearly states the fundamental principles of international convergence, the convergence process, the roles and responsibilities of all stakeholders, and the timeframe for international convergence.
- The establishment of good relationships with and cooperation among all stakeholders, including preparers, auditors, users of financial statements, governments, and regulators.
- The consideration of the effect that international convergence may have on small- and medium-sized entities and accounting firms.
- The establishment of a formal translation process, which involves both professional translators and professional accountants.
- The alignment of national standard-setting agendas and processes with those of the international standard setters.
- The devotion of significant resources to working with and influencing the work of the international standard setters.

standards and IFRSs. (Many participants were of the view, however, that, when entering into such agreements, the international standard setters' focus should remain on the development of globally accepted high quality standards.)

National standard setters are encouraged to publish formal international convergence strategies, addressing matters such as the fundamental principles of convergence, the convergence process, the roles and responsibilities of the various stakeholders, and a timeframe for implementing their strategies. Translation issues (see next page) should also be addressed.

National standard setters are further encouraged to cover the criteria for additional national requirements as a fundamental principle in their formal international convergence strategies. Such additional requirements

should be limited to those necessary as a result of national laws and regulations. National best practices not dealt with in the international standards should be communicated to and considered by the international standard setters.

In addition, national standard setters should consider how best to incorporate the additional national requirements in the adopted international standards. Varied approaches have been reported. For example, the exposure draft of the UK APB clearly differentiates additional material from the ISA content, while in the case of the French and German auditing standards, which incorporate the ISAs, the additional material is not separately differentiated. Clear differentiation of the additional national requirements is preferred since it facilitates easy maintenance of the adopted international standards and of the additional national requirements, and enables preparers or auditors who wish to comply with IFRSs or ISAs to distinguish the additional national requirements from the IFRSs or ISAs.

It is also recommended that regional professional accountancy organizations take actions to facilitate the adoption and implementation of the international standards. It has been recognized that the adoption and implementation of the international standards often has similar consequences for countries in the same region, and thus, solutions may be found at a regional level.

Well organized and resourced regional professional accountancy organizations could assist national professional accountancy bodies and national standard setters by combining efforts to adopt and implement the inter-

national standards. They could facilitate input to the international standard-setting processes, translation of the international standards, and the education and training of preparers, auditors, and users of financial statements.

IFAC member bodies have an important role to play as well. IFAC has created a Member Body Compliance Program, which is designed to encourage IFAC member bodies to adopt and implement the international standards. The Statements of Membership Obligations are the foundation of the Member Body Compliance Program. They are designed to provide clear benchmarks to current and potential IFAC member bodies to assist them in ensuring high-quality performance by professional accountants worldwide.

Additionally, IFAC has established the Developing Nations Permanent Task Force to support the development of the accountancy profession in developing nations by aiding their participation in the international standard-setting process and their efforts of seeking resources from other IFAC member bodies and other organizations in developing nations. □

**NATIONAL** *standard setters are encouraged to make international convergence the core of their work and the focus of their resources.*

## TRANSLATION OF THE INTERNATIONAL STANDARDS



The translation of the international standards is a major challenge in the adoption and implementation of the standards. Translators often find it difficult to convey the real meaning of the English text in the translated standards. Issues that were noted by participants as contributing to the difficulty of translation were the following:

- The use of lengthy English sentences;
- Inconsistent use of terminology;
- The use of the same terminology to describe different concepts; and
- The use of terminology that is not capable of translation. For example, international standards use words such as “shall” and “should” and the present tense to indicate different levels of obligations, while many languages are not capable of using the same indicators.

Most participants also felt that the international standards should be written in simple English that can better accommodate translations.

Another issue with respect to translations is the consistent use of terminology in the translated standards. To address this issue, some translators, in the first instance, have translated the international standard setters’ glossary of terms, or some other list of key words. Some participants, however, were of the view that the IAASB’s glossary of terms did not contain all the words that were thought to be “key.” Mention was made of such concepts as “significant” or “material” which might well have different nuances in different languages, as well as being concepts that might be subject to cultural differences and influences.

### *Impact of Funding*

Participants reported that donor funding is frequently used to support the translation of the international standards. Since this funding sometimes covers a one-time or specific project, organizations do not always have the resources to support the translation of new and revised international standards. Considering the frequency and volume of changes to the international standards, the translated standards soon become outdated, and preparers and auditors of financial statements can no longer claim compliance with the IFRSs and ISAs respectively.

### *Timetable for Translations*

Concern was expressed that IFRSs endorsed by the European Commission and effective in the EU on January 1, 2005 may not all be translated in a time-frame that will allow for proper implementation. The Commission has indicated that it may take nine months from the publication of an IFRS by the IASB until the translated standard is available in the Official Journal of the Commission.

Participants also raised timing issues with respect to the international exposure drafts. Some national standard setters issue the international exposure drafts, or national exposure drafts incorporating the international exposure drafts, at the same time that they are issued by the international standard setters. This enables them to consider the comments received on a national level and to respond to the international standard setter. However, this may not be possible where the time allowed for submitting comments is short and does not take account of the time required to translate these exposure drafts.

### *Involvement of Professional Accountants*

The majority of participants emphasized the importance of involving professional accountants in the translation of the international standards. There was also a concern that, should a translation of the international standards not involve the developers or users of the international standards, it may compromise the quality of the translation.

### Conclusions and Proposed Actions

The International Accounting Standards Committee (IASC) Foundation has established a translation process for IFRSs, and in July 2004, the IFAC Board approved a Policy Statement on *Translation of Standards and Guidance Issued by the International Federation of Accountants*. It is hoped that these initiatives will facilitate high quality translations of the international standards. In addition, it was recommended that IFAC establish on its website a forum through which issues pertaining to translation might be reported and solutions shared, and that future exposure drafts of proposed international standards ask whether any issues might arise regarding translation of the standards.

To ensure consistency in translations and maximize available resources, countries that speak the same language are encouraged to coordinate their efforts and, over time, eliminate the existence of multiple translations of international standards into the same language. The French translation of the ISAs led by the Instituut der Bedrijfsrevisoren – Institut des Reviseurs d'Entreprises (Belgium) and involving representatives of its counterparts in France, Canada, and more recently Luxembourg and

Switzerland, have proved beneficial to all parties in achieving a common understanding and translation of key words.

With respect to translations of international exposure drafts, it was recommended that consideration be given to adding a 30-day period between when an international exposure draft is made available to national standard setters and when it is issued both internationally and nationally. This would allow national standard setters to translate the international exposure draft, insert a preface, and incorporate the necessary additional national requirements. Comments received on the exposure draft could then be considered at both a national and international level.

A national standard setter reported that it performs “rough” translations of proposed ISAs before final approval of the ISAs by the IAASB. This facilitates earlier implementation.

Finally, it is recommended that regional professional accountancy organizations take an active role in the facilitation of translations. Their involvement could help prevent duplication of effort and contribute to the release of timely and high quality translations. Additionally, efforts on their part to secure funding for translations could help make translated standards more broadly available. □

**MOST** participants felt that the international standards should be written in simple English that can better accommodate translations.

### SUCCESS FACTORS

Factors that contributed to national professional accountancy bodies' success in translating the international standards include:

- The development of a formal translation plan and establishment of a translation team that includes professional accountants.
- To ensure the consistent use of terminology, the translation of a list of key words in the first instance and, where appropriate, obtaining the input of translators of the international standards in other countries that speak the same language.
- Actively seeking and securing donor or other funding that not only covers the initial translation of the international standards, but also the translation of new and revised standards.
- The establishment of a translation process that provides for the early translation of proposed and final international standards, enabling earlier implementation of the standards.

## COMPLEXITY AND STRUCTURE OF THE INTERNATIONAL STANDARDS



Participants were of the view that the international standards are increasingly becoming longer, more complex, and rules-based, and that the structure and complexity of the standards are affecting, largely in an adverse way, both their adoption and implementation. In particular, reference was made to the international accounting standards on financial instruments and the international auditing standards on audit risk, fraud, and quality control. Despite the comments on length and level of detail, a need for more implementation guidance was generally supported.

The international regulators, however, appeared to be supportive of the longer and more detailed ISAs issued recently. The length of and detail in the ISAs provide for a tighter regulatory environment and consistent application of the ISAs.

Participants emphasized the importance of applying a principles-based approach in international standard setting. It was felt that standards that are long, complex, and rules-based are difficult to implement and are likely to result in a compliance and avoidance mentality.

Participants reported that the international standard setters appear to have little or no sympathy for the fact that some countries need to incorporate their adopted international standards in national law or regulation. The international standards are not written in the form of law or regulation and, therefore, have to be “transformed” by the national standard setters. Or, as is the case in a country that incorporates the ISAs in its national auditing standards, the obligations are incorporated in national law or regulation and the explanatory text is incorporated in pronouncements issued by the national professional accountancy body.

A participant cautioned national standard setters against the above-mentioned approach since it may affect the authority of the national standards. For example, the obligations incorporated in national law or regulation may be authoritative, while the explanatory text published elsewhere may not be authoritative. It is, therefore,

important to consider the hierarchy of national standards in comparison with the authority attached to the international standards.

Some participants also had difficulties understanding the ordering of text in the international auditing standards since the logic of the structure was not always clear to them. An example cited was the practice in ISAs of placing an obligation on the auditor, followed by definitions of terminology included in the obligation, and then explaining the obligation. Some participants felt that these steps should be treated in a different order.

Adding to the complexity of IFRSs is the IASB’s move towards a fair value model. Many participants were of the view that fair value is a subjective concept and is difficult to measure accurately – different interpretations could lead to different conclusions. However, the

investment professionals, who believe that the IASB is not going far enough in its fair value model, were of the view that the matter could be overcome by explaining the effect that fair valuation has on the financial position and results of operations in the financial statements. For example, the

volatility caused by fair valuation could be disclosed in a separate section of shareholders’ funds. The market (and regulators) will then know how to deal with this.

### *Conclusions and Proposed Actions*

It is recommended that the international standard setters become more attuned to the challenges national standard setters and preparers, auditors, and users of financial statements face in adopting and implementing the international standards. In particular, participants recommended that international standard setters develop standards that continue to be principles based, the text of which is not complex, and the structure of which lends itself to incorporation in national law or regulation and to implementation.

The IAASB has taken a first step in this regard. It has undertaken a project to clarify the language and style of its pronouncements. The objective is to issue pronouncements that are understandable by those who perform the relevant engagements and are clear and capable of consistent application. □

**PARTICIPANTS** *emphasized the importance of applying a principles-based approach in international standard setting.*

## FREQUENCY, VOLUME, AND COMPLEXITY OF CHANGES TO THE INTERNATIONAL STANDARDS



It has clearly been a very challenging time for preparers, auditors, and users of financial statements – not only as a result of new and revised international standards, but also because of the many new requirements emanating from parties

other than the accounting and auditing standard setters. Participants questioned whether the cumulative effect of these changes on the preparers, auditors, and users of financial statements is being monitored by those who set the requirements. A participant recommended that the following question should be asked about every change: Will the value added exceed the cost to implement the change?

The frequency, volume, and complexity of the changes to the international standards are evidenced by the following:

- The IASB's Improvements Project, which gave rise to 13 standards being amended simultaneously with consequential amendments to many others (598-page document issued by the IASB in December 2003).
- Repeated changes of the same standards, including changes reversing IASB's previous stand and changes for the purpose of international convergence. These include changes to the international accounting standards on presentation of financial statements; accounting policies, changes in accounting estimates and errors; property plant and equipment; the effects of changes in foreign exchange rates; and financial instruments.
- Complex changes requiring considerable technical expertise. These include changes to the international accounting standards on financial instruments, impairment of assets, and employee benefits.

*IT is equally important for the international standard setters to strike a balance between the need to improve the international standards on a priority basis and the need to address the practical issue of providing countries with the time they need to adopt and implement these standards.*

- Changes to the IAASB's audit risk model, which gave rise to three new international auditing standards and consequential amendments to many others.
- New international standards on quality control, dealing with quality control at the accounting firm and audit engagement levels.
- A revised international auditing standard on the auditor's responsibility to consider fraud in an audit of financial statements, published in February 2004, while a previous revision of the same standard became effective for audits of financial statements for periods ending on or after June 30, 2002.

Given the above, national standard setters may decide not to adopt international standards that are subject to change in the near future. For example, the UK ASB proposes not to incorporate certain IFRSs in its national accounting standards. There are a number of different reasons for its decision. On cost/benefit grounds it does not wish to issue a national accounting standard that incorporates a relevant international standard,

which is likely to change significantly in the near future.

Furthermore, as discussed earlier, in some countries the adopted international standards are incorporated in national law or regulation. Consequently, national law or regulation has to be revised every time the international standards are revised.

Also, due to frequent changes to the international standards, "real life examples" of best practice are not readily available to users of these standards.

Participants acknowledged that the international standard setters are working diligently to improve the international standards as soon as possible, with January 1, 2005 as an important target date for the IASB. However,

they reported that it is equally important for the international standard setters to strike a balance between the need to improve the international standards on a priority basis and the need to address the practical issue of providing countries with the time they need to adopt and implement these standards. For example, allowing a short period of time to implement a complex IFRS that requires significant changes to an entity's financial reporting system or a complex ISA that requires significant changes to audit methodologies and training can undermine progress towards international convergence.

### *Conclusions and Proposed Actions*

It is recognized that the international standards need to be responsive to market changes, the needs of investors, and diverse and complex financial products. However, given the frequency, volume, and complexity of changes to the international standards, the international standard setters should consider how they can effectively and efficiently accommodate national efforts to adopt and implement these standards.

The IASB achieved its target of issuing new standards and revising existing standards intended to apply to accounting periods beginning on or after January 1, 2005 by March 31, 2004. This allows entities in the EU, and in other countries that have committed to the adoption of IFRSs in 2005, at least some lead-time to transition to this IFRS “stable platform.”

Furthermore, the IAASB is considering a “quiet period” for adoption and implementation of IASs. This quiet period would provide users of IASs a time during which no new or revised IASs will become effective. While the IAASB will continue to develop new or revise existing ISAs, those issued during the quiet period will not become effective before the end of the quiet period.

Going forward, it is recommended that the international standard setters collect information regarding a realistic adoption and implementation timetable for national standard setters and preparers, auditors, and users of financial statements. This should be factored into their standard-setting processes and the determination of the effective dates of new and revised international standards.

Furthermore, the implementation of the international standards is not only an accounting issue – it is also a business issue. Consequently, anticipated changes to the international standards should be considered at an early stage by the preparers of the financial statements and the potential effect thereof discussed with all interested parties, including those charged with governance of the entity. □

### **SUCCESS FACTOR**

Matters relating to the frequency of changes to the international standards are being addressed. In preparing their international convergence timetable, national standard setters delay the adoption of those international standards that are under revision until such time as they are finalized. This prevents changes to a national standard shortly after incorporation of an international standard.



## CHALLENGES FOR SMALL- AND MEDIUM-SIZED ENTITIES AND ACCOUNTING FIRMS



In most countries, many or even all entities are required by national law or regulation to prepare financial statements that conform to a required set of generally accepted accounting principles, and for these financial statements to

be audited in accordance with a required set of generally accepted auditing standards. These audited financial statements are normally filed with a government agency and thus are available to creditors, suppliers, employees, governments, and others. A large number of these entities are small- and medium-sized entities. In Europe, for example, it is estimated that there are about 7,000 public interest entities and more than one million private entities. (While the European Commission is calling for only listed entities that prepare consolidated financial statements to comply with IFRSs, it is possible that all public interest and private entities will be audited under ISAs beginning in 2007.)

Virtually all participants raised issues concerning the relevancy and appropriateness of the international standards to small- and medium-sized entities and accounting firms. Key concerns expressed were as follows:

- Length and complexity of the international standards;
- Cost of compliance with IFRSs versus benefits obtained;
- Inconsistent application of the international standards;
- Perceived focus on large-entity issues; and
- Lack of sufficient small- and medium-sized entity and accounting firm representation on the international standard-setting boards.

Comments on these issues are described further below.

Some national standard setters already seem to be working individually to determine how best to provide for financial reporting by small- and medium-sized entities in their national laws, regulations, or standards.

These individual national approaches were not viewed as efficient and participants suggested that they would only pose a risk to international convergence. Additionally, comparability and consistency would be compromised if alternative approaches exist. Consequently, participants felt that it was very important for the IASB's project to develop international accounting standards for small- and medium-sized entities to progress rapidly, with sufficient and appropriate input from small- and medium-sized entities.

With respect to ISAs, participants were of the view that the focus of ISAs has changed from the audits of financial statements of entities of all sizes to the audits of financial statements of large, complex, public interest, and often multi-national entities. The ISAs are progressively

becoming more difficult to apply to the audits of financial statements of small- and medium-sized entities. The international auditing standards dealing with audit risk were mentioned as an example.

There was also a sense that the international

standard setters do not recognize or appreciate the effect that changes in the fundamental principles of the international standards have on small- and medium-sized entities and accounting firms. The financial statements of small- and medium-sized entities are often used as the basis for tax preparation, banking covenants, and other reporting requirements. A whole re-education process, which extends beyond the preparers and auditors of financial statements to users, such as investors, lenders, tax authorities, and regulators, is necessary as a result of these changes.

**VIRTUALLY** all participants raised issues concerning the relevancy and appropriateness of the international standards to small- and medium-sized entities and accounting firms.

A participant indicated that the small- and medium-sized segment needs to be further segmented to distinguish the very small from the rest. “IFRS light” or “ISA light” may not be appropriate for very small entities. Consequently, a different set of standards may have to be developed for a third segment – where financial reporting is mainly for tax authorities and banks.

### *Conclusions and Proposed Actions*

In June 2004, the IASB issued a discussion paper on *Preliminary Views on Accounting Standards for Small- and Medium-Sized Entities*. The purpose of the discussion paper is to invite comments on the IASB’s preliminary views on its basic approach to develop international accounting standards for small- and medium-sized entities.

The IASB’s project was recognized as a significant step in addressing the needs of small- and medium-sized entities and participants encouraged the IASB to progress this project rapidly.

National standard setters and preparers, auditors, and users of financial statements of small- and medium-sized entities are encouraged to respond to the above-mentioned IASB discussion paper and to comment on relevant proposed pronouncements issued by the IASB and IAASB.

The IAASB has established a process to obtain the input of IFAC’s Small and Medium Practices Permanent Task Force on small- and medium-sized entity audit considerations to be incorporated in new and revised pronouncements.

The October 2004 European Congress for SME and SMP Accountants, organized by FEE, with the co-operation of Arc Méditerranéen des Auditeurs (hosted by Instituto de Censores Jurados de Cuentas de España), and featuring speakers from the IASB and IFAC, along with European leaders, is another important action. Activities such as these that provide a forum for dialogue between the international and national standard setters and small- and medium-sized entities and accounting firms are encouraged and much needed.

Finally, but most significantly, on an ongoing basis, the international and national standard setters should ensure that the needs of small- and medium-sized entities and accounting firms are addressed in the development of the international standards. For example, a participant recommended that ISAs be written with the simplest audit in mind and considerations for large, complex public interest entities should be added where necessary. Involving representatives from small- and medium-sized entities and accounting firms in the standard-setting process is seen as critical. □

## SUCCESS FACTORS

Factors that contributed to addressing successfully the needs of small- and medium-sized entities include:

- National standard setters including representatives from small- and medium-sized entities and accounting firms on their boards.
- National standard setters and professional accountancy bodies liaising with governments, regulators, and other interested parties to provide for differential reporting by small- and medium-sized entities.
- Small- and medium-sized accounting firms using the longer and more detailed ISAs to train their staff and to implement the ISAs.

## POTENTIAL KNOWLEDGE SHORTFALL



### *Awareness, Knowledge, and Skills*

The increasing proliferation and complexity of global issues, transactions, financial products, and standards present new challenges to the accountancy profession to ensure that it has the requisite knowledge and skills to carry out its responsibilities. In particular, there appears to be a potential knowledge shortfall with respect to the international standards.

Education and training were considered major challenges by most of the participants. They were of the view that only very few professional accountants have a detailed knowledge of IFRSs and the requisite skills to apply them.

For example, the results of a survey of members from business and practice conducted by the Institute of Chartered Accountants in England and Wales in June 2003 on the awareness of, and preparation for, the introduction of the international accounting standards revealed the following:

- A third of the respondents were either “not very aware” or “not aware at all” of the publication of the European Union’s regulation on the application of the international accounting standards;<sup>2</sup>
- Less than half of the respondents felt they were aware of the effect that the international accounting standards would have on their organization or its financial statements;
- Two thirds of the respondents were either “not very aware” or “not aware at all” of the IASB’s project timetable; and
- Only a quarter of the respondents knew what the UK ASB’s views and aims were in relation to the international convergence process.

The results of a recent PricewaterhouseCoopers survey<sup>3</sup> of more than 300 European companies show that just 10% of survey participants are confident they have the right people and skills in place to complete the transitions to IFRSs in the EU on time. Smaller entities, in particular, are finding it difficult to commit full-time resources to the implementation of IFRSs. The concern for entities is whether the people they need will be

available as the demand for IFRS specialists reaches its peak in 2004/2005.

The World Bank, in preparing the *Reports on the Observance of Standards and Codes*, found that developing and emerging economies with no existing national standards find it most easy and appealing to adopt the international standards. However, due to a lack of knowledge of the international standards, and often capacity, they find it most difficult to implement them.

Some participants were concerned about over-reliance on the technical expertise in accounting firms. Entities that do not have the technical expertise are becoming more dependent on their auditors to interpret the IFRSs.

Implementation of the ISAs by networks of accounting firms should be easier due to the development and

implementation of global audit methodologies and training programs incorporating ISAs as well as global internal inspection programs to monitor compliance with the standards.

Although many countries have incorporated the inter-

national standards in the education and training of students, a participant was concerned about educators’ knowledge of the international standards since they normally are not involved in the implementation of these standards.

Another participant was of the view that the volume and speed of changes made it impossible for students to develop the skill and ability to apply the international standards. This participant reported a decline in students’ ability to deal with problems critically and analytically. Students should be taught how to apply a framework of principles to different circumstances – for the detail, they could refer to the handbooks of international standards.

Participants were also concerned about the knowledge of analysts and the media. Participants representing professional investors, however, were of the view that analysts will be prepared for the transition to IFRSs.

### *A Need for Interpretations*

There is a need for an easier and quicker way to resolve matters of interpretation of IFRSs. Participants commented on the need for the IASB and, in particular, the International Financial Reporting Interpretations Committee (IFRIC), to be more cooperative in this regard.

**URGENT** attention should be given to the development of implementation guidance that is widely available to all in need of such guidance.

<sup>2</sup> Regulation (EC) No 1606/2002, July 19, 2002.

<sup>3</sup> International Financial Reporting Standards: Ready to Take the Plunge?, May 2004.

Participants were of the view that, at present, some IFRSs are open to varying interpretations and competitors are “shopping” for more favorable interpretation on common issues. To prevent this, some industries have started to organize forums where leading entities could discuss their approaches to common issues.

#### *A Need for Implementation Guidance*

Participants reported a need for implementation guidance. They were of the view that implementation guidance is of particular importance when the international standards are applied for the first time, when there are translation issues, and when there is a lack of technical expertise and “real life examples” of best practice. In addition, reference was made to the implementation of the international standards in the context of, for example, national legal and regulatory frameworks and cultures.

#### *Conclusions and Proposed Actions*

National professional accountancy bodies are encouraged to continue to create an awareness and expand the knowledge of professional accountants and others of the international standards.

Educational institutions are encouraged to provide the educators with education and training in the international standards. They should also offer programs of accounting and auditing that produce accounting graduates familiar with the international standards.

For entities that are implementing IFRSs, an understanding of the standards is necessary from the top down – from those responsible for the governance of the entity to those responsible for financial and operational reporting by individual business units. Consequently, training programs should involve individuals at all levels of the entity and should continue after the initial transition to IFRSs.

There is also a need to make analysts and journalists aware of the effect that the transition to IFRSs may have on entities’ financial statements. Participants encouraged entities to provide analysts with the information necessary to interpret their entities’ financial positions and results of operations.

The international standard setters are encouraged to establish processes, or enhance existing processes, to respond to requests for interpretations in a timely manner.

Furthermore, urgent attention should be given to the development of implementation guidance that is widely available to all in need of such guidance.

There was no consensus as to who should develop the implementation guidance. Possibilities include: the international standard setters, national standard setters, national professional accountancy bodies, and large accounting firms. However, if the guidance is developed by anyone other than the international standard setters, there may be a lack of international coordination and a corresponding lack of consistency. □

## SUCCESS FACTORS

Factors that contributed to addressing successfully the potential knowledge shortfall include:

- National professional accountancy bodies offering training to their members by way of seminars, and large entities and accounting firms providing compulsory training to their staff.
- National professional accountancy bodies educating analysts and journalists on the effect that the transition to IFRSs may have on an entity’s financial statements. This includes the issuance of press releases and posting of information on websites.
- Educational institutions involving staff from accounting firms in teaching the international standards.
- International organizations that represent industries, such as financial institutions, providing training to their members by way of seminars.
- Industries organizing forums where leading entities can discuss challenges and solutions to implementing specific IFRSs.
- Entities, viewing the transition to IFRSs as a business issue and not just an accounting issue, training staff at all levels, including those outside the financial reporting system, for example, staff responsible for determining the effect of new international accounting standards on an entity’s remuneration policies.

## IMPLICATIONS OF ENDORSEMENT OF IFRSs



As those in the EU and other countries continue to prepare to meet their upcoming deadlines for the adoption of the international accounting standards, they are faced with unique challenges, some of which are discussed in more detail below.

### *Two Sets of Accounting Standards*

It is possible that after January 1, 2005 two very different sets of accounting standards may apply in the same EU member state, i.e., IFRSs and national accounting standards. The European Union's regulation on the application of international accounting standards<sup>4</sup> limits the mandatory adoption of IFRSs to listed entities that prepare consolidated financial statements. However, it provides for EU member states to decide whether to adopt IFRSs for other entities.

Some EU member states are amending national law or regulation to provide for compliance with IFRSs or national accounting standards by other entities, while others have decided to continue to require compliance with national accounting standards.

Although national laws or regulations and the irrelevancy and inappropriateness of IFRSs to small- and medium-sized entities were cited as some reasons for maintaining national accounting standards, the existence of two sets of standards has potential negative implications. Most obvious is the use of national accounting standards in the individual financial statements and IFRSs in the consolidated financial statements of the same entity. Also, students and preparers, auditors, and users of financial statements will have to know two sets of accounting standards.

### *Limited Application to Listed Entities*

As discussed earlier, the European Union's regulation limits the adoption of IFRSs to listed entities that prepare consolidated financial statements. Participants were concerned about other public interest entities, such as financial institutions, that may not be listed.

### *Potential Late Endorsement or Non-endorsement of IFRSs*

Participants indicated that the European Commission's potential late endorsement or non-endorsement of the international accounting standards on financial instruments is creating uncertainties for preparers, auditors, and users of financial statements.

There are serious implications if non-endorsement of some IFRSs result in a European standard in one or more areas. FEE cites the following implications in its *FEE Position – Call for Global Standards: IFRS* (June 2004):

- Extra disclosures to explain differences from IFRSs, for reasons of transparency.
- Entities would no longer be able to claim that their financial statements were prepared in accordance with IFRSs, with related consequences for the audit and the auditor's report.
- The effect that any unique European standard may have on financial reporting systems. For example, changes with regard to the recognition, measurement, and disclosure of complex financial instruments.
- A risk that some entities, such as financial institutions, that apply or want to apply the non-endorsed IFRS will be seriously disadvantaged.
- Access to capital markets could be restricted or made more expensive.
- A loss of opportunity to converge IFRSs and U.S. accounting standards and possible effect on other elements of transatlantic dialogue.
- A risk of setting a precedent.

Referring to the potential late endorsement or non-endorsement of the international accounting standards on financial instruments, participants were concerned about the politicians' role in international standard setting. This concern is well summarized in a speech of Bob Herz, chair of the U.S. FASB at a conference of the American Institute of Certified Public Accountants and the U.S. Securities Exchange Commission held in December 2003 (his references are to both the IASB and FASB): *"All our constituents, including politicians, have a very legitimate interest in our activities. But I believe that*

*interest must be in our properly fulfilling our mission of establishing sound, neutral accounting standards and not in trying to bias our activities and decisions through pressure and threatened intervention into our independent and, we believe, objective process ... Standard setting should not be a political process because the primary objective must be on the relevance, reliability, and usefulness of reported information and not on trying to satisfy the favored economic, business, social, or political goals of particular interest groups ...”*

**Preparedness for the Adoption of the International Standards**

The results of the recent PricewaterhouseCoopers survey<sup>5</sup> of more than 300 European companies indicate that, given the greater risks involved, large entities have made more progress towards implementation of the IFRSs than smaller ones. Also, financial services companies were slightly further advanced with their preparations. According to the survey results, this could be because they are intensely affected by the international accounting standards on financial instruments.

The results of the survey set out seven steps that entities need to work through in order to embed IFRSs, and indicated the degree to which those surveyed have achieved them.

In Australia, which is also working towards the implementation of IFRSs on January 1, 2005, a survey of 122 corporations conducted by the Institute of Chartered Accountants in Australia (ICAA) in July 2004, has revealed that less than half of those surveyed (49%) have commenced the implementation process for IFRSs. However, the percentage of respondents preparing for the implementation of IFRSs would grow to 84% within the next six months.

One of the most critical issues for entities will be explaining to investors and analysts how their financial position and results of operations will differ under IFRSs compared with their previously applied national accounting standards. The PricewaterhouseCoopers survey found that 80% of entities had not organized their communications plans. According to the ICAA survey, only 35% of respondents have started to communicate to stakeholders the effect of IFRSs on the financial position and results of their entities.

The Committee of European Securities Regulators (CESR) has recommended that entities provide markets with appropriate and useful information in a phased process. For example, it is recommended that a narrative of IFRS transition progress and key accounting differences between previously applied national accounting standards and IFRSs be included with the 2003 financial statements.

STEP	ACTION	PROGRESS
1	Assess the high-level impact of IFRSs on the business (at least preliminary assessment)	75%
2	Decide on accounting policies (at least for high priority areas)	46%
3	Identify the missing data	26%
4	Enhance systems to collect data (at least for high priority areas)	11%
5	Put processes in place to ensure data collected is robust	10%
6	Design internal controls to demonstrate reliability of data	10%
7	Embed IFRSs and use for internal management reporting	11%

<sup>5</sup> International Financial Reporting Standards: Ready to Take the Plunge?, May 2004.

### *Conclusions and Proposed Actions*

As the deadline for the adoption of IFRSs approaches in the EU and other countries, such as Australia, it is critical for all stakeholders to identify and address any outstanding matters.

Referring to the discussion paper on *UK Accounting Standards: A Strategy for Convergence with IFRS* as an example, a participant recommended that national standard setters in countries that offer entities other than listed entities the option to comply with IFRSs or national accounting standards should have formal international convergence strategies. Working towards one set of accounting standards, they should evaluate their national accounting standards to identify differences between the national accounting standards and IFRSs, and actively contribute to the international standard-setting process. (This could equally be applied to countries that do not offer the option, as the ultimate goal should be international convergence – i.e., one set of globally accepted accounting standards.)

Governments or regulators should consider the application of IFRSs to public interest entities that are not listed and that do not prepare consolidated financial statements.

**REGULATORS** *should consider the application of IFRSs to public interest entities that are not listed and that do not prepare consolidated financial statements.*

Ongoing dialogue regarding any delay in the endorsement or non-endorsement of a particular international standard is necessary so that all stakeholders could plan accordingly and a contingency plan, addressing concerns of regulators and the relevant international standard setter, could be developed and agreed.

Furthermore, entities that are planning to or have adopted IFRSs are encouraged to actively contribute to the international standard-setting process, in particular to identify practical implementation issues.

Entities that are planning to adopt IFRSs are encouraged to identify differences between the previously applied national accounting standards and IFRSs, design and implement an IFRS transition program, and address required financial reporting system changes. They should also provide training to staff at all levels.

Additionally, professional accountancy bodies, national standard setters, and entities that are planning to or have adopted IFRSs should clearly communicate to the users of the financial statements, including analysts and journalists, the effect of the adoption of IFRSs on entities' financial positions and results of operations. Local seminars could be held in this regard. □

## PROPOSALS FOR ACTIONS BY STAKEHOLDERS



**A**ction is necessary at all points along the information supply chain that delivers financial reporting. Governments, regulators, international and national standard setters, reporting entities, and

auditors, as well as other participants in the financial reporting process, have important roles to play in international convergence.

Actions needed to support international convergence are highlighted below.

### *Governments and Regulators*

- Establish legal and regulatory environments that provide for compliance with all the international standards, with no or very limited additional national requirements.
- Write or revise laws and regulations to reflect the international standards and international best practice.
- Designate financial reporting laws and regulations as a high priority and act within a reasonable period of time.
- Establish efficient and effective enforcement mechanisms to increase the consistency and quality of compliance with the international standards.

### *International Standard Setters (IASB and IAASB)*

- Establish a process, or enhance the existing process, whereby national standard setters, in aligning their agendas with that of the international standard setters, have an opportunity to actively contribute to the international standard-setting processes.
- As a matter of urgency, develop standards in a manner that takes account of small- and medium-sized entity financial reporting and audit considerations. In addition, provide for greater small- and medium-sized entity and accounting firm representation.
- Address concerns about the complexity and structure of the international standards.
- Write standards in simple English that is understandable, clear, and capable of translation and consistent application.

- In developing the international standards and setting effective dates, be cognizant of the fact that proposed and final standards are being translated in some countries that are adopting them.
- In considering changes to the international standards, be cognizant of the cost vs. the benefits of the proposed changes.
- Establish a process, or enhance the existing process, to respond in a timely manner to requests for interpretations.
- Consider the development of implementation guidance.
- Provide, or continue to provide, unlimited access to all authoritative pronouncements and implementation guidance.
- Institute a “quiet period” for the adoption and implementation of the international standards.

### *National Standard Setters*

- Develop a formal international convergence strategy and obtain the commitment of all stakeholders.
- Develop an active standard-setting agenda, which is aligned with that of the international standard setters and aimed at eliminating existing differences with the international standards. This should be achieved within a reasonable period of time.
- Establish a process, or enhance the existing process, to actively contribute to the international standard-setting processes, including the development of international standards for small- and medium-sized entities and accounting firms.

### *Reporting Entities*

- Design and implement an IFRS transition program and allocate the necessary resources. This includes obtaining the commitment from the top down, i.e., from those charged with governance to those responsible for financial reporting by individual business units. Also consider the interdependencies between the transition to IFRSs and other financial reporting projects, such as compliance with national laws and regulations.



- Prepare to implement IFRSs by identifying differences and addressing required financial reporting system changes.
- Design and implement plans to change management reporting used to monitor the performance of the business from the previously applied national accounting standards to IFRSs.
- Provide IFRS training for staff at all levels affected by the transition to IFRSs.
- Develop an external communications strategy.
- Actively contribute to the international standard-setting process, in particular, to identify practical implementation issues.
- Consider at an early stage anticipated changes to the international standards and discuss with all interested parties the changes' potential effect on the financial statements.

#### *Auditors*

- Raise an awareness of the international standards among clients.
- Align audit methodologies and training with the international standards.
- Provide IFRS and ISA training to staff at all levels.

#### *Analysts and Investors*

- Promote convergence of the national standards with the international standards.
- Actively contribute to the international standard-setting processes, in particular to identify users' needs.
- Provide IFRS training to staff at all levels.

#### *International Federation of Accountants*

- Study and further develop the concept of “international convergence,” i.e., when has a country achieved convergence of its national standards with the international standards.
- Establish a process that facilitates translation of the international standards.

- Monitor and enforce compliance with IFAC's Statements of Membership Obligations.
- Assist member bodies with the development of action plans to ultimately achieve compliance with the Statements of Membership Obligations.

#### *Regional Professional Accountancy Organizations*

- Coordinate contributions to the international standard-setting processes, translations of the international standards, and training in the international standards at a regional level.

#### *National Professional Accountancy Bodies*

- Facilitate the adoption and implementation of the international standards through compliance with IFAC's Statements of Membership Obligations.
- In line with the Statements of Membership Obligations, assist government, regulators, and the national standard setters in formulating and enacting convergence of the national and international standards, and in addressing impediments to international convergence (e.g., tax reporting vs. financial reporting).
- Support the preparation of high quality translations of the international standards.
- In line with the Statements of Membership Obligations, create awareness and expand the knowledge of students, professional accountants, and others of the international standards.
- Establish processes that facilitate maximum contribution to the international standard-setting processes – representing the views of professional accountants and others on all relevant issues.

#### *Educational Institutions*

- Educate and train the educators in the international standards.
- Offer programs of accounting and auditing that produce accounting graduates familiar with the international standards.

## SUMMARY AND CONCLUSIONS



Listening to national standard setters and preparers, auditors, and users of financial statements, it is clear that there are many challenges to achieving international convergence.

As mentioned earlier in the report, all those involved in the financial reporting process will need to take action. Much of this action is highlighted in the Proposals for Action by Stakeholders section on pages 23 and 24.

As progress on international convergence continues, particularly in the EU, it is vital that there be frequent open and ongoing dialogue between regulators, international standard setters, and national standard setters and that these groups continue to listen to the concerns and needs of those who will have to implement the standards. Significant consideration should be given to the effect of international convergence on small- and medium-sized entities and accounting firms.

The greatest challenge for the participants was “preparing or preparedness for the adoption of the international standards.” What must be done nationally? What support, if any, can be expected from the international standard setters? How will national ini-

tiatives to achieve international convergence affect the reporting entities in a country, and what actions should be taken nationally to address these effects, and who should take these actions? How can the education and training of professional accountants keep pace with the changing environment in which the international standards are being set? Who will keep investors, analysts, journalists, and members of the public informed of these changes and their consequences?

As international convergence progresses, questions like these will continue to be raised. All those working to achieve international convergence – from IFAC to regional and national professional accountancy organizations to international and national standard setters

and international and national regulators – can and should help to resolve the challenges.

Most importantly, we all need to remember that convergence to a single set of globally accepted high quality standards is ultimately in the best interests of the public, contributing to efficient capital

flows within countries and across borders. In the views of the majority of participants, international convergence is vital to economic growth. Thus, while the challenges are great, the rewards are potentially even greater. □

**WE** all need to remember that convergence to a single set of globally accepted high quality standards is ultimately in the best interests of the public.

## APPENDIX 1: LIST OF FOCUS GROUP MEETINGS, INTERVIEWS, AND RESPONDENTS



Written submissions were received from:

Association of Chartered Certified Accountants  
 Association of Professional Accountants and Auditors  
 of the Republic of Moldova  
 Auditing Standards Committee of the Institute of  
 Chartered Accountants in Ireland  
 Britannia Building Society (United Kingdom)  
 Certified General Accountants Association of Canada  
 Chartered Institute of Public Finance  
 and Accountancy  
 Consiglio Nazionale dei Dottori Commercialisti  
 (Italy)  
 Federación Argentina de Consejos Profesionales de  
 Ciencias Económicas (Argentina)  
 Föreningen Auktoriserade Revisorer (Sweden)  
 KHT-yhdistys - Föreningen CGR ry (Finland)  
 Hong Kong Institute of Certified Public Accountants  
 Howarth Central America  
 HTM-tilintarkastajat ry (Finland)  
 Institut der Wirtschaftsprüfer (Germany)  
 Institute of Certified Public Accountants in Israel  
 Institute of Certified Public Accountants of Singapore  
 Institute of Chartered Accountants in Australia and  
 CPA Australia  
 Institute of Chartered Accountants in England  
 and Wales  
 Institute of Chartered Accountants of India  
 Institute of Professional Accountants of Russia  
 Instituto de Censores Jurados de Cuentas  
 de España (Spain)  
 Instituto Mexicano de Contadores Públicos,  
 A.C. (Mexico)  
 Instituut der Bedrijfsrevisoren – Institut des  
 Réviseurs d'Entreprises (Belgium)  
 Japanese Institute of Certified Public Accountants  
 Koninklijk Nederlands Instituut van Register-  
 accountants (The Netherlands)  
 Malaysian Institute of Accountants  
 Malaysian Institute of Certified Public Accountants  
 National Board of Chartered Accountants of the  
 Accountants Association in Poland  
 PricewaterhouseCoopers

Focus group meetings were arranged by the following:

Chartered Institute of Management Accountants  
 Confederation of Asian and Pacific Accountants  
 Eastern Central and Southern African Federation  
 of Accountants  
 Fédération des Experts Comptables Européens –  
 Audit Working Party  
 Fédération des Experts Comptables Européens –  
 Financial Reporting Policy Group  
 IFAC Small and Medium Practices Permanent  
 Task Force  
 Instituto dos Auditores Independentes  
 do Brasil (Brazil)  
 Inter-American Accounting Association  
 United Kingdom Resident Members of the Analyst  
 Representative Group

Interviews were held with representatives from  
 the following:

Accounting and Auditing Standard Setters  
 in Australia  
 Accounting and Auditing Standard Setters  
 in Canada  
 Accounting and Auditing Standard Setters  
 in Denmark  
 Accounting and Auditing Standard Setters  
 in South Africa  
 Accounting Standard Setter in the United Kingdom  
 Basel Committee on Banking Supervision  
 Professional Oversight Board for Accountancy  
 (United Kingdom)  
 Transnational Auditors Committee  
 World Bank



## APPENDIX 2: LIST OF QUESTIONS COVERED IN FOCUS GROUP MEETINGS, INTERVIEWS, AND WRITTEN SUBMISSIONS



These questions were asked in relation to both the pronouncements issued by the IASB and the pronouncements issued by the IAASB.

- To what degree do you consider that the international standards have been adopted in your country?
- Has the structure or complexity of the international standards affected their adoption or implementation? If so, how?
- Does the legal process for adoption of the international standards in your country cause any impediment to adoption? If so, to what extent?
- Is there enough lead time to allow for adoption of the international standards?
- If you have had to translate the international standards from English, have there been issues of clarity of the original text? If so, how have these been addressed?
- Are there any issues pertaining to the applicability of the international standards to listed entities, small- and medium-sized entities, and not-for-profit organizations? What issues have been raised and how have they been addressed?
- To what extent do you think that professional accountants are knowledgeable of the content of the international standards? Are there any concerns that need to be addressed? If so, how?
- Are there any concerns regarding students' knowledge of the content of the international standards? How is this being addressed?
- Are the consequences of adopting the international standards acceptable to users?



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