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Accounting Advisory Services

Challenges in converging to IFRS for SOEs

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Around the globe ……

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IFRS – the global landscape

June 2002

EU adoption of regulation requiring all listed EU groups to apply IFRS in their financial statements by 1 January 2005

2002 – 2008 and going on ……

Over 100 countries on IFRS

2011

150 countries expected to adopt IFRS

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Why Global convergence?

Benefits for companies

- Improved management information for decision making
- Better access to capital, including from foreign source
- Reduced cost of capital
- Ease of using one consistent reporting standard in subsidiaries from different countries/comparison of SOEs across countries
- Facilitated mergers and acquisitions
- Enhanced competitiveness

Benefits for investors

- Better information for decision making
- More confidence in the information presented
- Better understanding of risk and return
- Companies can be compared to a peer group of companies

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Why Global convergence?

Benefits for policy makers

- Strengthened and more effective Indian capital market
- Better access to the global capital markets
- Promotion of cross-border investment

Benefits for national regulatory bodies

- Improved regulatory oversight and enforcement
- A higher standard of financial disclosure
- Better information for market participants to underpin disclosure-based regulation
- Better ability to attract and monitor listings by foreign companies

Benefits for other stakeholders

- Greater credibility and improved economic prospects for the accounting profession.
- Enhanced transparency of companies through better reporting
- Better reporting and information on new and different aspects of the business

The Indian landscape IFRS convergence

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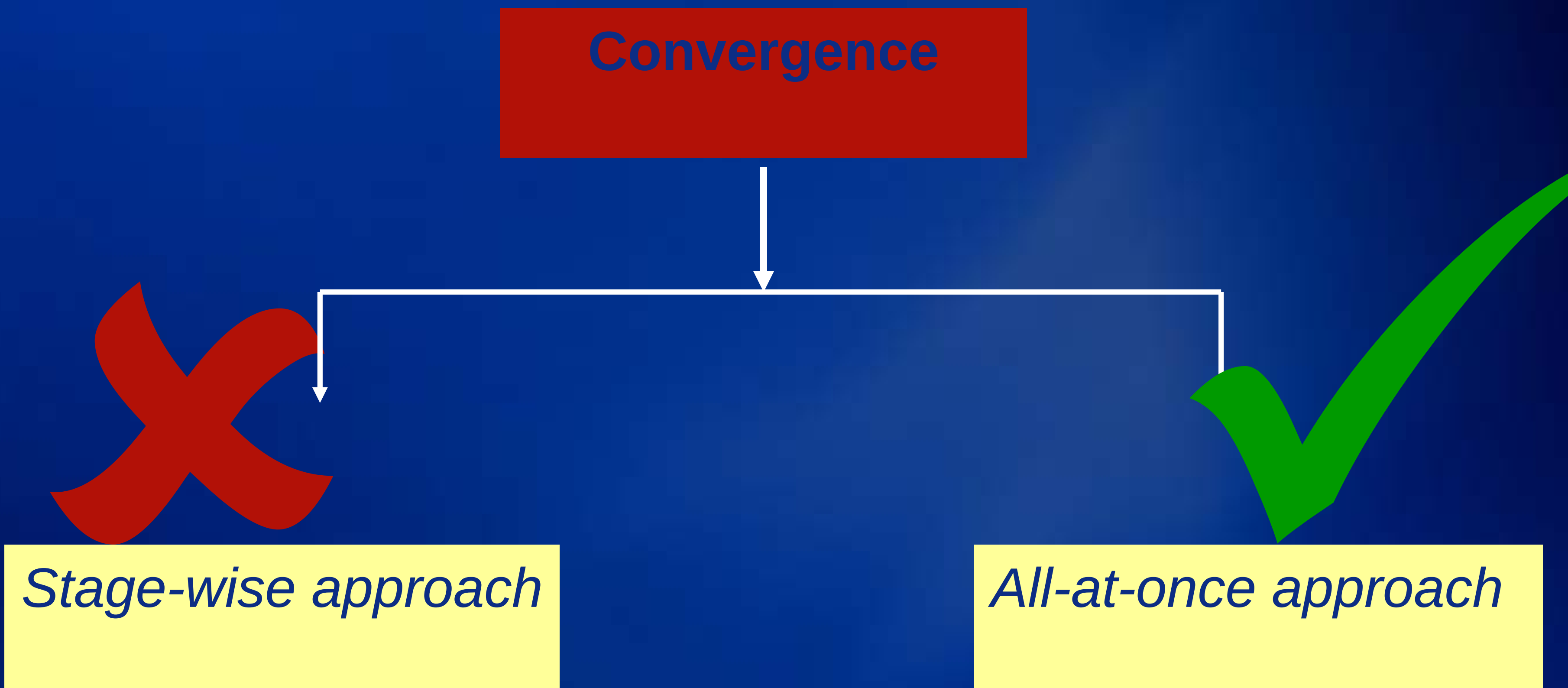
IFRS convergence in India – applicability

- **Applicable to public interest entities for accounting years commencing 1 April 2011 onwards**
  - Listed entities
  - Banks, mutual funds, insurance entities
  - Other large-sized entities (Turnover exceeds Rs 100 crore or public/bank borrowings exceed Rs 25 crore)
  - Holding and subsidiary companies of the above entities

ICAI's approach to convergence



On adoption of IFRSs -
Where standards are in conflict with the laws / regulations, the latter will prevail

India implementation challenges ……..

- **Regulatory challenges**
  - Government
  - Regulators e.g., SEBI, RBI and IRDA
  - Taxation laws
  - Courts/Tribunal
- **Economic environment**
- **Trained/Qualified accounting professionals**
- **Educating academics, accountants, issuers, regulators and investors**

Further Challenges in SOE

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Some key impact areas – presentation and accounting

- Components/Presentation of Financial statements
- Use of fair values – relevance over reliability
- Business Combinations
- Detailed guidance on treatment of government grants
- Extensive disclosure requirements

Anticipating the challenge to solve it faster ….

- Key decision makers to adopt principles
- Availability of IFRS technical resources
- Cost of bridging gaps in knowledge – budget constraints
- Organization wide training in IFRS principles relevant to entity
- IFRS 1 (still to be adopted by ICAI) may also require going back in time to evaluate impact – unless record retention is reasonably effective just gathering information could be a challenge
- Applying fair values to accounting

So what is involved in IFRS convergence?........

Do you want to consider looking at IFRS whollistically?

What are the differences in accounting and disclosures between current and future GAAP?

How does IFRS impact my systems and processes?

What are further impacts of the IFRS implementation?

What are the needs for training and how can training be provided?

How does the Conversion Plan look like?
What are the impacts on resources / budget?

… structured and efficient!

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Multiple impacting areas to consider…….

- Accounting gap analysis
- Tax impact analysis
- Reporting gap analysis
- Alternative accounting treatments
- Financial and business impact assessment
- Measures to reduce potential volatility

- IT/process impact assessment
- Systems/process conversion strategy
- Initial IFRS awareness training
- Management presentations
- IFRS project plan and budget

Some factors that would affect …..

- New system vs. modify existing systems
- Changes at group, company or source system levels
- Dual reporting requirements
- Cutover approach from local GAAP general ledger to IFRS general ledger
- Harmonising internal and external reporting

Lessons learned: typical pitfalls

- **Rapid start to implementing work without a structured assessment**
- **Time to complete and/ or resources are underestimated: "We will just switch to IFRS"**
- **Accounting rules are seen as "pretty similar", but small differences can matter a lot**
- **Impacts of IFRS conversion are not addressed with stakeholders**
  - Lack of clarity about strategies for selecting the various accounting options
  - Inability to provide information on all areas impacted by IFRS (e.g. to analysts)
- **Lack of sufficient communication with auditors**

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Key take aways

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Conclusion

- Understand the IFRS impact early in the project lifecycle – accounting, process, people and IT
- Complexities not to be underestimated – it cannot be done in isolation
- Not just a finance project – adopt a holistic approach
- Post conversion activities – the hard work may just be beginning – develop a sustainable approach

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