This IFRS Supplement provides expanded discussions of accounting guidance under International Financial Reporting Standards (IFRS) for the topics in Intermediate Accounting. The discussions are organized according to the chapters in Intermediate Accounting (13th or 14th Editions) and therefore can be used to supplement the U.S. GAAP requirements as presented in the textbook. Assignment material is provided for each supplement chapter, which can be used to assess and reinforce student understanding of IFRS.

**GLOBAL MARKETS**

World markets are becoming increasingly intertwined. International consumers drive Japanese cars, wear Italian shoes and Scottish woolens, drink Brazilian coffee and Indian tea, eat Swiss chocolate bars, sit on Danish furniture, watch U.S. movies, and use Arabian oil. The tremendous variety and volume of both exported and imported goods indicates the extensive involvement in international trade—for many companies, the world is their market.

To provide some indication of the extent of globalization of economic activity, Illustration 1-1 provides a listing of the top 20 global companies in terms of sales.

<table>
<thead>
<tr>
<th>Rank ($ millions)</th>
<th>Company</th>
<th>Country</th>
<th>Revenues ($ millions)</th>
<th>Rank ($ millions)</th>
<th>Company</th>
<th>Country</th>
<th>Revenues ($ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Wal-Mart Stores</td>
<td>U.S.</td>
<td>378,799.0</td>
<td>11</td>
<td>Daimler</td>
<td>Germany</td>
<td>177,167.1</td>
</tr>
<tr>
<td>2</td>
<td>ExxonMobil</td>
<td>U.S.</td>
<td>372,824.0</td>
<td>12</td>
<td>General Electric</td>
<td>U.S.</td>
<td>176,656.0</td>
</tr>
<tr>
<td>3</td>
<td>Royal Dutch Shell</td>
<td>Netherlands</td>
<td>355,782.0</td>
<td>13</td>
<td>Ford Motor</td>
<td>U.S.</td>
<td>172,468.0</td>
</tr>
<tr>
<td>4</td>
<td>BP</td>
<td>U.K.</td>
<td>291,438.0</td>
<td>14</td>
<td>Fortis</td>
<td>Belgium/Netherlands</td>
<td>164,877.0</td>
</tr>
<tr>
<td>5</td>
<td>Toyota Motor</td>
<td>Japan</td>
<td>230,200.8</td>
<td>15</td>
<td>AXA</td>
<td>France</td>
<td>162,762.3</td>
</tr>
<tr>
<td>6</td>
<td>Chevron</td>
<td>U.S.</td>
<td>210,783.0</td>
<td>16</td>
<td>Sinopec</td>
<td>China</td>
<td>159,259.6</td>
</tr>
<tr>
<td>7</td>
<td>ING Group</td>
<td>Netherlands</td>
<td>201,516.0</td>
<td>17</td>
<td>Citigroup</td>
<td>U.S.</td>
<td>159,229.0</td>
</tr>
<tr>
<td>8</td>
<td>Total</td>
<td>France</td>
<td>187,279.5</td>
<td>18</td>
<td>Volkswagen</td>
<td>Germany</td>
<td>149,054.1</td>
</tr>
<tr>
<td>9</td>
<td>General Motors</td>
<td>U.S.</td>
<td>182,347.0</td>
<td>19</td>
<td>Dexia Group</td>
<td>Belgium</td>
<td>147,648.4</td>
</tr>
<tr>
<td>10</td>
<td>ConocoPhillips</td>
<td>U.S.</td>
<td>178,558.0</td>
<td>20</td>
<td>HSBC Holdings</td>
<td>U.K.</td>
<td>146,500.0</td>
</tr>
</tbody>
</table>


In addition, due to technological advances and less onerous regulatory requirements, investors are able to engage in financial transactions across national borders and to make investment, capital allocation, and financing decisions involving many foreign companies. Also, many investors, in attempts to diversify their portfolio risk, have invested more heavily in international markets. As a result, an increasing number of investors are holding securities of foreign companies. For example, over a recent seven-year period, estimated investments in foreign equity securities by U.S. investors increased over 20-fold, from $200 billion to $4,200 billion.

An indication of the significance of these international investment opportunities can be found when examining the number of foreign registrations on various securities exchanges. As shown in Illustration 1-2, a significant number of foreign companies are found on national exchanges.

As indicated, capital markets are increasingly integrated and companies have greater flexibility in deciding where to raise capital. In the absence of market integration, there can be company-specific factors that make it cheaper to raise capital and list/trade securities in one location versus another. With the integration of capital markets, the automatic linkage between the location of the company and location of the
capital market is loosening. As a result, companies have expanded choices of where to raise capital, either equity or debt. The move toward adoption of international financial reporting standards has and will continue to facilitate this movement.

### STANDARD-SETTING ORGANIZATIONS

For many years, many nations have relied on their own standard-setting organizations. For example, Canada has the Accounting Standards Board, Japan has the Accounting Standards Board of Japan, Germany has the German Accounting Standards Committee, and the United States has the Financial Accounting Standards Board (FASB). The standards issued by these organizations are sometimes principles-based, rules-based, tax-oriented, or business-based. In other words, they often differ in concept and objective. Starting in 2000, two major standard-setting bodies have emerged as the primary standard-setting bodies in the world.

One organization is based in London, United Kingdom, and is called the International Accounting Standards Board (IASB). The IASB issues International Financial Reporting Standards (IFRS), which are used on most foreign exchanges. These standards may also be used by foreign companies listing on U.S. securities exchanges. As indicated earlier, IFRS is presently used in over 115 countries and is rapidly gaining acceptance in other countries as well.

The other standard-setting organization is the Financial Accounting Standards Board (FASB), which is based in the United States. All U.S.-based companies are required to use FASB standards when preparing financial statements and related financial information. Some note that FASB standards are more comprehensive and detailed, whereas IASB standards are more conceptual and less rules-based. Regardless of viewpoint, both Boards believe that a single set of high-quality global accounting standards is needed to enhance comparability.

It is generally believed that IFRS has the best potential to provide a common platform on which companies can report and investors can compare financial information. As a result, our discussion focuses on IFRS and the organization involved in developing these standards—the International Accounting Standards Board (IASB). The two organizations that have a role in international standard-setting are the International Organization of Securities Commissions (IOSCO) and the IASB.

### International Organization of Securities Commissions (IOSCO)

International Organization of Securities Commissions (IOSCO) does not set accounting standards. Instead, this organization is dedicated to ensuring that the global markets can operate in an efficient and effective basis. The member agencies (such as from France, Germany, New Zealand, and the U.S. SEC) have resolved to:

- Cooperate together to promote high standards of regulation in order to maintain just, efficient, and sound markets.
• Exchange information on their respective experiences in order to promote the development of domestic markets.
• Unite their efforts to establish standards and an effective surveillance of international securities transactions.
• Provide mutual assistance to promote the integrity of the markets by a rigorous application of the standards and by effective enforcement against offenses.

A landmark year for IOSCO was 2005 when it endorsed the IOSCO Memorandum of Understanding (MOU) to facilitate cross-border cooperation, reduce global systemic risk, protect investors, and ensure fair and efficient securities markets. (For more information, go to http://www.iosco.org/.)

International Accounting Standards Board (IASB)

The standard-setting structure internationally is composed of four organizations—the International Accounting Standards Committee Foundation, the International Accounting Standards Board (IASB), a Standards Advisory Council, and an International Financial Reporting Interpretations Committee (IFRIC). The trustees of the International Accounting Standards Committee Foundation (IASC) select the members of the IASB and the Standards Advisory Council, fund their activities, and generally oversee the IASB’s activities.

The IASB is the major operating unit in this four-part structure. Its mission is to develop, in the public interest, a single set of high-quality and understandable IFRS for general-purpose financial statements. In addition to research help from its own staff, the IASB relies on the expertise of various task force groups formed for various projects and on the Standards Advisory Council (SAC). The SAC consults with the IASB on major policy and technical issues and also helps select task force members. IFRIC develops implementation guidance for consideration by the IASB. We discuss the IFRIC’s activities in more detail below. Illustration 1-3 shows the current organizational structure for the setting of international standards.

Due Process

In establishing financial accounting standards, the IASB has a thorough, open, and transparent due process. The IASB due process has the following elements: (1) an independent standard-setting board overseen by a geographically and professionally
Furthermore, the characteristics of the Board, as shown below, reinforce the importance of an open, transparent, and independent due process.

- **Membership.** The membership consists of 14 members, two who are part-time. Members are well-paid and appointed for five-year renewable terms. The 14 members come from different countries.
- **Autonomy.** The IASB is not part of any other professional organization. It is appointed by and answerable only to the International Accounting Standards Committee Foundation.
- **Independence.** Full-time IASB members must sever all ties from their past employer. The members are selected for their expertise in standard-setting rather than to represent a given country.
- **Voting.** Nine of 14 votes are needed to issue a new IFRS.

With these characteristics, the IASB and its members will be insulated as much as possible from the political process, favored industries, and national or cultural bias.

**Types of Pronouncements**

The IASB issues three major types of pronouncements:

2. Framework for financial reporting.
3. International financial reporting interpretations.

**International Financial Reporting Standards.** Financial accounting standards issued by the IASB are referred to as International Financial Reporting Standards (IFRS). The
IASB has issued nine of these standards to date, covering such subjects as business combinations and share-based payments.

Prior to the IASB (formed in 2001), standard-setting on the international level was done by the International Accounting Standards Committee, which issued International Accounting Standards (IAS). The committee issued 40 IASs, many of which have been amended or superseded by the IASB. Those still remaining are considered under the umbrella of IFRS.

**Framework for Financial Reporting.** As part of a long-range effort to move away from the problem-by-problem approach, the International Accounting Standards Committee (predecessor to the IASB) issued a document entitled “Framework for the Preparation and Presentation of Financial Statements” (also referred to simply as the Framework). This Framework sets forth fundamental objectives and concepts that the Board uses in developing future standards of financial reporting. The intent of the document is to form a cohesive set of interrelated concepts—a conceptual framework—that will serve as tools for solving existing and emerging problems in a consistent manner. For example, the objective of general-purpose financial reporting discussed earlier is part of this Framework. The Framework and any changes to it pass through the same due process (discussion paper, public hearing, exposure draft, etc.) as an IFRS. However, this Framework is not an IFRS and hence does not define standards for any particular measurement or disclosure issue. Nothing in this Framework overrides any specific international accounting standard. The Framework is discussed more fully in Chapter 2.

**International Financial Reporting Interpretations.** Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) are also considered authoritative and must be followed. These interpretations cover (1) newly identified financial reporting issues not specifically dealt with in IFRS, and (2) issues where unsatisfactory or conflicting interpretations have developed, or seem likely to develop, in the absence of authoritative guidance. The IFRIC has issued over 15 of these interpretations to date.\(^1\)

In keeping with the IASB’s own approach to setting standards, the IFRIC applies a principles-based approach in providing interpretative guidance. To this end, the IFRIC looks first to the Framework for the Preparation and Presentation of Financial Statements as the foundation for formulating a consensus. It then looks to the principles articulated in the applicable standard, if any, to develop its interpretative guidance and to determine that the proposed guidance does not conflict with provisions in IFRS.

IFRIC helps the IASB in many ways. For example, emerging issues often attract public attention. If not resolved quickly, they can lead to financial crises and scandal. They can also undercut public confidence in current reporting practices. The next step, possible governmental intervention, would threaten the continuance of standard-setting in the private sector. IFRIC can address controversial accounting problems as they arise. It determines whether it can resolve them or whether to involve the IASB in solving them. In essence, it becomes a “problem filter” for the IASB. Thus, the IASB will hopefully work on more pervasive long-term problems, while the IFRIC deals with short-term emerging issues.

**Hierarchy of IFRS**

Because it is a private organization, the IASB has no regulatory mandate and therefore no enforcement mechanism. Similar to the U.S. setting, in which the Securities and Exchange Commission enforces the use of FASB standards for public companies, the

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\(^1\)As indicated above, the predecessor organization to the IASB was also involved in the standard-setting process. It had an interpretations committee called the Standing Interpretation Committee, which issued 32 interpretations (a number of these are now superseded).
IASB relies on other regulators to enforce the use of its standards. For example, effective January 1, 2005, the European Union required publicly traded member country companies to use IFRS.²

Any company indicating that it is preparing its financial statements in conformity with IFRS must use all of the standards and interpretations. The following hierarchy is used to determine what recognition, valuation, and disclosure requirements should be used. Companies first look to:

1. International Financial Reporting Standards;
2. International Accounting Standards; and
3. Interpretations originated by the International Financial Reporting Interpretations Committee (IFRIC) or the former Standing Interpretations Committee (SIC).

In the absence of a standard or an interpretation, the following sources in descending order are used: (1) the requirements and guidance in standards and interpretations dealing with similar and related issues; (2) the framework for financial reporting; and (3) most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature, and accepted industry practices, to the extent they do not conflict with the above. The overriding requirement of IFRS is that the financial statements provide a fair presentation (often referred to as a “true and fair view”). Fair representation is assumed to occur if a company follows the guidelines established in IFRS.

**International Convergence**

As discussed in the opening story, convergence to a single set of high-quality financial reporting standards appears to be a real possibility. For example, in 2002 the IASB and the FASB formalized their commitment to the convergence of U.S. GAAP and international standards by issuing a memorandum of understanding (often referred to as the Norwalk Agreement). The two Boards agreed to use their best efforts to:

1. Make their existing financial reporting standards fully converged as soon as practicable, and
2. Coordinate their future work programs to ensure that once achieved, convergence is maintained.

As a result of this agreement, the two Boards identified a number of short-term and long-term projects that would lead to convergence. For example, one short-term project was for the FASB to issue a standard that permits a fair value option for financial instruments. This standard was issued in 2007, and now the IASB and the FASB follow the same accounting in this area. Conversely, the IASB has issued a standard related to borrowing costs that is more consistent with U.S. standards. Long-term projects relate to such issues as revenue recognition, the conceptual framework, and leases.

²Certain changes have been implemented with respect to use of IFRS in the United States. For example, under American Institute of Certified Public Accountants (AICPA) rules, a member of the AICPA can only report on financial statements prepared in accordance with standards promulgated by standard-setting bodies designated by the AICPA Council. In May 2008, the AICPA Council voted to designate the IASB in London as an international accounting standard-setter for purposes of establishing international financial accounting and reporting principles, and to make related amendments to its rules to provide AICPA members with the option to use IFRS.
QUESTIONS

1. What is happening to world markets, and what are the implications for financial reporting?
2. What is the benefit of a single set of high-quality accounting standards?
3. Who are the two key international players in the development of international accounting standards? Explain their role.
4. What is the purpose of IOSCO?
5. What is the mission of the IASB?

6. How are IASB discussion papers and IASB exposure drafts related to IASB standards?
7. Distinguish between IASB standards and the IASB framework for financial reporting.
8. Rank from most authoritative to least authoritative the following three items: IASB framework for financial reporting, IASB financial reporting standards, and international financial reporting interpretations.

CONCEPTS FOR ANALYSIS

CA1-1 (IFRS and Standard-Setting) Presented below are five statements which you are to identify as true or false. If false, explain why the statement is false.

1. The IASB uses a rules-based approach to its standard-setting process, whereas the FASB uses a principles-based approach.
2. The objective of financial statements emphasizes a stewardship approach for reporting financial information.
3. The purpose of the objective of financial reporting is to prepare a statement of financial position, a comprehensive income statement, a cash flow statement, and a statement of changes in equity.
4. The difference between International Accounting Standards and IFRS is that International Accounting Standards are rules-based instead of principles-based.
5. The objective of financial reporting uses an entity rather than a proprietary approach in determining what information to report.

CA1-2 (Financial Reporting and Accounting Standards) Answer the following multiple-choice questions.

1. IFRS stands for:
   (a) International Federation of Reporting Services.
   (b) Independent Financial Reporting Standards.
   (c) International Financial Reporting Standards.
   (d) Integrated Financial Reporting Services.

2. The major key players on the international side are the:
   (a) IASB and FASB.
   (b) IOSCO and the SEC.
   (c) SEC and FASB.
   (d) IASB and IOSCO.

3. Which body from the U.S. side is similar to the IASB?
   (a) SEC.
   (b) FASB.
   (c) FASC.
   (d) FAF.

4. Accounting standard-setters use the following process in establishing international standards:
   (a) Research, exposure draft, discussion paper, standard.
   (b) Discussion paper, research, exposure draft, standard.
   (c) Research, preliminary views, discussion paper, standard.
   (d) Research, discussion paper, exposure draft, standard.

5. IFRS is comprised of:
   (a) International Financial Reporting Standards and FASB financial reporting standards.
   (c) International Accounting Standards and international accounting interpretations.
   (d) FASB financial reporting standards and International Accounting Standards.

6. The authoritative status of the Framework for Financial Reporting is as follows:
   (a) It is used when there is no standard or interpretation related to the reporting issues under consideration.
   (b) It is not as authoritative as a standard but takes precedence over any interpretation related to the reporting issue.
(c) It takes precedence over all other authoritative literature.
(d) It has no authoritative status.

7. The objective of financial reporting places most emphasis on:
(a) reporting to capital providers.
(b) reporting on stewardship.
(c) providing specific guidance related to specific needs.
(d) providing information to individuals who are experts in the field.

8. General-purpose financial statements are prepared primarily for:
(a) internal users.
(b) external users.
(c) auditors.
(d) government regulators.

9. Economic consequences of accounting standard-setting means:
(a) standard-setters must give first priority to ensuring that companies do not suffer any adverse effect as a result of a new standard.
(b) standard-setters must ensure that no new costs are incurred when a new standard is issued.
(c) the objective of financial reporting should be politically motivated to ensure acceptance by the general public.
(d) accounting standards can have detrimental impacts on the wealth levels of the providers of financial information.

10. The expectations gap is:
(a) what financial information management provides and what users want.
(b) what the public thinks accountants should do and what accountants think they can do.
(c) what the governmental agencies want from standard-setting and what the standard-setters provide.
(d) what the users of financial statements want from the government and what is provided.

CA1-3 (IASB Role in Standard-Setting) A press release announcing the appointment of the trustees of the new International Accounting Standards Committee Foundation stated that the International Accounting Standards Board (to be appointed by the trustees) “…will become the established authority for setting accounting Standards.”

Instructions
(a) Identify the sponsoring organization of the IASB and the process by which the IASB arrives at a decision and issues an accounting standard.
(b) Indicate the major types of pronouncements issued by the IASB and the purposes of each of these pronouncements.

USING YOUR JUDGMENT

FINANCIAL REPORTING

Financial Reporting Problem
Lola Otero, a new staff accountant, is confused because of the complexities involving accounting standard-setting. Specifically, she is confused by the number of bodies issuing financial reporting standards of one kind or another and the level of authoritative support that can be attached to these reporting standards. Lola decides that she must review the environment in which accounting standards are set, if she is to increase her understanding of the accounting profession.

Lola recalls that during her accounting education there was a chapter or two regarding the environment of financial accounting and the development of IFRS. However, she remembers that her instructor placed little emphasis on these chapters.

Instructions
(a) Help Lola by identifying key organizations involved in accounting rule-making at the international level.
(b) Lola asks for guidance regarding authoritative support. Please assist her by explaining what is meant by authoritative support.
Professional Research

As a newly enrolled accounting major, you are anxious to better understand accounting institutions and sources of accounting literature. As a first step, you decide to explore the IASB's Framework for the Preparation of Financial Statements.

Instructions

Access the IASB Framework at the IASB website (http://eifrs.iasb.org/). When you have accessed the documents, you can use the search tool in your Internet browser to respond to the following items. (Provide paragraph citations.)

(a) What is the objective of financial reporting?
(b) What other means are there of communicating information, besides financial statements?
(c) Indicate some of the users and the information they are most directly concerned with in economic decision-making.